TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 27

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

PAUL R. G. HORST

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED MARCH 2, 1940

CERTIORARI GRANTED APRIL 8, 1940

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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1 Before United States Board of Tax Appeals

Docket No. 90819

PAUL R. G. HORST, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances: For Taxpayer: Harry H. Wiggins, Esq. For Commissioner: J. R. Johnston, Esq.

Docket entries

1937

Sept. 24—Petition received and filed. Taxpayer notified (Fee paid).
Sept. 24—Copy of petition served on General Counsel.
Nov. 12—Answer filed by General Counsel.
Nov. 16—Copy of answer served on taxpayer.
Nov. 20—Motion for circuit hearing at New York, N. Y., filed by taxpayer. 11/22/37 granted.

1938

Nov. 16—Hearing set Jan. 9, 1939, in New York City.

1939

Jan. 9—Hearing had before Mr. Hill, Div. 2, on the merits. Submitted. Consolidated for hearing with Docket 93220. Stipulations of facts filed at hearing. Briefs due in 30 days, simultaneously.
Jan. 23—Transcript of hearing of Jan. 9, 1939, filed.
Feb. 3—Brief filed by General Counsel.
Feb. 7—Brief filed by taxpayer 2/7/39 copy served on General Counsel.
Feb. 21—Reply brief filed by taxpayer. 2/21/39 copy served on General Counsel.
Mar. 21—Motion for leave to file the attached supplemental reply brief, brief lodged filed by taxpayer. 3/21/39 Granted.
2 Mar. 21—Copy of motion and supplemental reply brief served on General Counsel.
Apr. 12—Findings of fact and opinion rendered, Sam B. Hill, Div. 2. Decision will be rendered for the respondent.
Apr. 17—Decision entered, Sam B. Hill, Div. 2.
June 30—Petition for review by United States Circuit Court of Appeals, Second Circuit, with assignments of error filed by taxpayer.
July 13—Proof of service filed.
July 13—Praecipe filed by taxpayer, with proof of service thereon.

Before United States Board of Tax Appeals

Docket No. 93220

PAUL R. G. HORST, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances: For Taxpayer: Harry H. Wiggins, Esq. For Commissioner: J. R. Johnston, Esq.

Docket entries

1938

Apr. 29—Petition received and filed. Taxpayer notified. (Fee not paid).

Copy of petition served on General Counsel.

May 4—Fee paid (Check).

May 5—Copy of petition served on General Counsel.

3 May 20—Answer filed by General Counsel.

May 20—Request for Circuit hearing in New York City filed by General Counsel.

May 27—Notice issued placing proceeding on New York City Calendar. Answer and request served on taxpayer.

Nov. 16—Hearing set Jan. 9, 1939, in New York City.

1939

Jan. 9—Hearing had before Mr. Hill, Div. 2, on the merits. Submitted. Consolidated for hearing with Docket 90819. Stipulations of facts filed at hearing. Briefs due in 30 days, simultaneously.

Jan. 23—Transcript of hearing of Jan. 9, 1939, filed.

Feb. 3—Brief filed by General Counsel.

Feb. 7—Brief filed by taxpayer. 2/7/39 copy served on General Counsel.

Feb. 21—Reply brief filed by taxpayer. 2/21/39 copy served on General Counsel.

Mar. 21—Motion for leave to file the attached supplemental reply brief, brief lodged filed by taxpayer. 3/21/39 Granted.

Mar. 21—Copy of motion and supplemental reply brief served on General Counsel.

Apr. 12—Findings of fact and opinion rendered, Sam B. Hill, Div. 2. Decision will be rendered for the respondent.

Apr. 17—Decision entered, Sam B. Hill, Div. 2.

June 30—Petition for review by United States Circuit Court of Appeals, Second Circuit, with assignments of error filed by taxpayer.

July 13—Proof of service filed.

July 13—Praecipe filed by taxpayer, with proof of service thereon.

4 Before United States Board of Tax Appeals

Docket No. 90819

[Titled omitted.]

Petition

Filed Sept. 24, 1937

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency dated June 26, 1937, and as a basis for this proceeding alleges upon information and belief:

I

The petitioner is a citizen of the United States temporarily residing at No. 3 Avenue Elisee Reclus, Paris, France.

II

The notice of deficiency (a copy of which is attached and marked Exhibit "A") was mailed to the petitioner on June 26, 1937.

III

The taxes in controversy are income taxes for the calendar year 1935 and the amount in controversy is $14,106.53. The deficiency asserted is $12,376.20, and the petitioner claims that he is entitled to a refund of $1,730.33, which amount was paid by the petitioner within two years before the filing of this petition.

IV

The determination of tax set forth in the said notice of deficiency is based upon the following error:

5 The inclusion in the petitioner's income of the sum of $25,495.00, representing the face value of negotiable coupons detached, transferred, and given before maturity by the petitioner to his son, Robert P. K. Horst as a gift.

V

The facts upon which the petitioner relies as the basis for this proceeding are as follows:

That on the dates hereinafter mentioned the petitioner detached, transferred, and delivered to his son, Robert P. K. Horst, as a gift, the following described negotiable coupons:

Face value of coupons	Name of bond	Due date of coupons	Date of gift
$2,616.25	U. S. of Brazil 6½s	Oct. 1, 1935	Aug. 21, 1935
$796.25	U. S. of Brazil 6½s	Oct. 15, 1935	Aug. 21, 1935
$3,282.50	City of Milan 6½s	Oct. 1, 1935	Aug. 21, 1935
$3,250.00	City of Rome 6½s	Oct. 1, 1935	Aug. 21, 1935
$2,800.00	U. S. of Brazil 7s	Dec. 1, 1935	Aug. 21, 1935
$2,750.00	City of Tokio 5½s	Oct. 1, 1935	Aug. 24, 1935
$3,000.00	City of Yokohama 6s	Dec. 1, 1935	Aug. 24, 1935
$7,000.00	Govt. of Italy 7s	Dec. 1, 1935	Aug. 24, 1935

Wherefore, the petitioner prays that this Board may hear the proceeding; that it may redetermine the liability of the petitioner for income taxes for the calendar year 1935; that in such redetermination it may find that there is an overpayment of income tax of $1,730.33 for said year and that such amount was paid by the petitioner within two years before the filing of this petition, and that it may grant such other and further relief as may be proper and just.

HARRY H. WIGGINS,
Attorney for Petitioner.

Office & Post Office Address: No. 15 Broad Street, Borough of Manhattan, New York City.

DUER, STRONG & WHITEHEAD,
of Counsel.

6 [*Duly sworn to by Harry H. Wiggins; jurat omitted in printing.*]

7 *Exhibit A to petition*

SN–N

TREASURY DEPARTMENT,
Washington, June 26, 1937.

Office of Commissioner of Internal Revenue.

Mr. PAUL R. G. HORST,
% Duer, Strong and Whitehead,
15 Broad Street, New York, New York.

SIR: You are advised that the determination of your income tax liability for the taxable year (s) ended December 31, 1935, discloses a deficiency of $12,376.20 as shown in the statement attached.

In accordance with section 272 (a) of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C1:P–7. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency and will

prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
Commissioner.
By CHAS. T. RUSSELL,
Deputy Commissioner.

Enclosures:
Statement.
Form 870.

8 STATEMENT

IT:A:2.
ABB–90D.

In re: Mr. Paul R. G. Horst, % Duer, Strong and Whitehead, 15 Broad Street, New York, New York

Tax Liability for Taxable Year Ended December 31, 1935: Income tax, liability, $40,441.66; assessed, $28,065.46; deficiency, $12,376.20.

The report of the Internal revenue agent in charge at 17 Battery Place, New York, New York, a copy of which was furnished you, is approved and is hereby made a part of this letter.

The revenue agent's findings were sustained after careful consideration of your protests dated February 1, 1937, and April 19, 1937, in connection with the findings of the examining officer and the information submitted at conferences held in the office of the internal revenue agent in charge on March 24, 1937, and May 14, 1937, respectively.

Your net income has been revised as follows:

Net income reported on your return		$97,171.22
Add:		
1. Other income	$22,360.00	
2. Taxes disallowed	14.87	
	22,374.87	
Deduct:		
3. Gain on collection of coupons reduced	84.20	
		22,290.67
Revised net income		119,461.89

9 Explanation of Changes

1. This office has sustained the revenue agent in his conclusion that $22,360.00, representing the value of interest coupons which you transferred before maturity to your son, Robert P. K. Horst, as a gift, is taxable to you.

In Porter v. United States Court of Claims, 52 Fed. (2d) 1056, the court held that dividends, interest, rent, or other income assigned by gift to charitable organizations, or others, without transfer of the

income-producing property or without loss of control thereof, remain taxable to the transferor though the income is paid to the transferee.

Income Tax Ruling 3011, published in Internal Revenue Bulletin, Volume XV, No. 42, dated October 19, 1936, holds as follows:

"Interest accrued on bonds prior to donation to a trust is income taxable to the settler and not to the beneficiaries even though the settler returns his income on the cash receipts and disbursements basis."

In the above ruling, it was held that the conclusion reached was justified by the fact that at the time the interest accrued the property from which it was derived belonged to the settler, and by the further fact that the settler's failure actually to receive accrued interest was due solely to the voluntary assignment of it to the beneficiaries of the trust.

In the instant case, the bonds were retained and the accrued interest voluntarily assigned to your son. For all practical purposes, it actually represented an assignment of income which is ordinarily held to be taxable to the assignor.

Your attention is invited to the fact that Income Tax Ruling 3011, referred to above, was promulgated subsequent to the decision in the case of Rosenwald v. Commissioner of Internal Revenue, Circuit Court of Appeals, 33 Fed. (2d) 423, upon which you rely and also subsequent to the stipulations entered into in your case for the years 1928 and 1929.

10 2. French income and property taxes were overstated by $14.87.

3. Gain realized on coupon collections was overstated by $84.20.

Computation of Tax

Revised net income		$119,461.89
Less: Personal exemption		2,500.00
Balance (surtax net income)		$116,961.89
Less:		
Dividends	$26,125.00	
Credit on earned net income (10% of $3,000.00)	300.00	
		26,425.00
Balance subject to normal tax		$90,536.89
Normal tax at 4% on $90,536.89		$3,621.48
Surtax on $116,961.89		36,820.18
Total tax		$40,441.66
Tax assessed, account #201446		28,065.46
Deficiency		$12,376.20

Expenses totaling $1,513.13, claimed on your return, have been allowed as a deduction from income.

In accordance with a request dated June 5, 1937, from Duer, Strong & Whitehead, this final notice of deficiency has been issued in accordance with section 272 of the Revenue Act of 1934.

A copy of this letter has been mailed to your representative, Mr. Harry H. Wiggins, % Duer, Strong & Whitehead, 15 Broad Street, New York, New York, in accordance with the authority contained in the power of attorney executed by you and on file with the Bureau.

11 Know all men by these presents: That I, Paul R. G. Horst, of 152 Carroll Street, Brooklyn, New York, have made, constituted, and appointed, and by these presents, do make, constitute, and appoint Selden Bacon, of Pleasantville, New York; Marshall Stearns, of New Canaan, Connecticut; Hugh Morgan, Jr., of West New Brighton, Richmond County, New York; Orwill V. W. Hawkins, of Plandome, Nassau County, New York; and Harry H. Wiggins, of Little Neck, Nassau County, New York, any or all of them, to be my true and lawful attorneys for me and in my name, place, and stead, to execute and file in my behalf amended returns, reports, claims for abatement, claims for refund, claims for credit, and any and all claims and other papers or documents, which may in any way affect or have any connection with any and all income-tax returns heretofore or hereafter filed by me and all income taxes at any time paid by me for the years covered by said returns or any additional income taxes claimed to be due under said income-tax returns or an account of income taxes covered by said returns, under the provisions of the Revenue Laws or other Statutes of the United States, and to appear for me before the Commissioner of Internal Revenue of the United States and any Board, Bureau, officers or other representatives of the Government of the United States or of any of its departments in connection with any of the aforesaid matters and to attend conferences, prepare and submit briefs, and make arguments in my behalf in connection therewith, to take appeals on my behalf to the United States Board of Tax Appeals relating to the aforesaid and sign the petition on said appeal, and any and all documents in any way connected with said appeal and to appear before said Board of Tax Appeals in my behalf, submit briefs, make arguments, and do all and everything in any way connected or relating to such an appeal and to receive and collect refunds and reclaims arising out of any of the aforesaid matters.

12 For better and more effectually executing the powers and authorities aforesaid, to do and perform all and every act and thing whatsoever requisite and necessary to be done in and about the premises as fully to all intents and purposes as I might or could do, if personally present at the doing thereof, with full power of substitution and revocation, hereby ratifying and confirming all that my said attorneys shall lawfully do or cause to be done by virtue hereof. This authority to remain in full force until revoked by me.

I hereby revoke the power of attorney given by me to William H. Van Benschoten, dated and acknowledged the 6th day of July 1926.

In witness whereof, I have hereunto set my hand and seal the 27 day of Aug., in the year of Our Lord, one thousand nine hundred and thirty.

PAUL R. G. HORST.

GERMAN REICH, STATE OF BAVARIA,
Consulate General of the
United States of America at Munich, ss:

Be it known, That on this 27th day of One thousand nine hundred and thirty, at the City of aforesaid, before me a Consul General of the United States of America, dwelling in said City of Munich, personally came and appeared Paul R. G. Horst, to me known, and known to me to be the individual described in, and who executed the foregoing instrument, and he acknowledged to me that he executed the same.

In testimony whereof, I have hereunto set my hand and affixed the Consular Seal of the United States of America at the City of Munich aforesaid, the day and year last above written.

[CONSULAR SEAL] CHARLES M. HATHAWAY, Jr.,
Charles M. Hathaway, Jr.,
Consul General of the United States of America.

Fee No. 45. Service No. 2506. U. S. Gold. No fee.

13 Before United States Board of Tax Appeals

Docket No. 90819

[Title omitted.]

Answer

Filed Nov. 12, 1937

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

I. Admits the allegations contained in Paragraph I of the petition.

II. Admits the allegations contained in Paragraph II of the petition.

III. Admits that the taxes in controversy are income taxes for the calendar year 1935 and that the deficiency asserted by respondent is $12,376.20; but denies the remaining allegations contained in Paragraph III of the petition.

IV. Denies that respondent's determination is erroneous as alleged in Paragraph IV of the petition.

V. Admits the allegations of fact contained in Paragraph V of the petition.

14 Denies generally and specifically each and every allegation contained in the petition and not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the appeal be denied.

(Signed) J. P. WENCHEL,
J. P. Wenchel,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:
CHESTER A. GWINN,
CHARLES E. LOWERY,
Special Attorneys,
Bureau of Internal Revenue.

Before United States Board of Tax Appeals

Docket No. 93220

[Title omitted.]

Petition

Filed April 29, 1938

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Rev-
15 enue in his notice of deficiency dated March 7, 1938, and as a basis for this proceeding, alleges upon information and belief:

I

The petitioner is a citizen of the United States, temporarily residing at No. 3 Avenue Elisee Reclus, Paris, France.

II

The notice of deficiency (a copy of which is hereto attached, marked Exhibit "A" and made a part hereof) was mailed to the petitioner on March 7, 1938.

III

The taxes on controver'y are income taxes for the calendar year 1934 and the amount in controversy is $13,903.09.

IV

The determination of tax set forth in the said notice of deficiency is based upon the following error:

The inclusion in the petitioner's income of the sum of $25,182.50, representing the face value of negotiable coupons detached, transferred, and given before maturity by the petitioner to his son, Robert P. K. Horst, as a gift.

V

The facts upon which the petitioner relies as the basis for this proceeding are as follows:

That the said sum of $25,182.50, included in the petitioner's income by the respondent, represents the face value of negotiable interest coupons hereinafter described, and that on the dates hereinafter
16 mentioned, the said coupons were detached, transferred, and delivered, before maturity, by the petitioner to his son, Robert P. K. Horst, as a gift, to wit:

Face value of coupons	Name of bond	Due date of coupons (1934)	Date of gift (1934)
$3,500.00	Tobe Elec. Pr. Co. 7s	Sep. 15	Aug. 16
$3,500.00	Ujigawa Elec. Pr. Co. 7s	Sep. 15	Aug. 16
$3,282.50	City of Milan 6½s	Oct. 1	Aug. 16
$3,250.00	City of Rome 6½s	Oct. 1	Aug. 16
$2,750.00	City of Tokio 5½s	Oct. 1	Aug. 16
$3,000.00	City of Yokohama 6s	Dec. 1	Aug. 16
$4,500.00	Tokio Elec. Lt. Co. 6s	Dec. 15	Aug. 16
$1,400.00	Kingdom of Italy 7s	Dec. 1	Aug. 16

Wherefore the petitioner prays that this Board may hear the proceeding; that it may redetermine the liability of the petitioner for the deficiency in income taxes for the year 1934 asserted by the respondent; that in such redetermination it may find that the coupons, described in Paragraph V hereof, detached, transferred, and given before maturity by the petitioner to his son, Robert P. K. Horst, are not taxable income as against him; that there is no deficiency due from the petitioner for the year 1934; and that your petitioner may have such other and further relief as may be proper and just.

HARRY H. WIGGINS,
Harry H. Wiggins,
Attorney for Petitioner.

Office and P. O. Address, No. 15 Broad Street, Borough of Manhattan, New York City, N. Y.

DUER, STRONG & WHITEHEAD,
of Counsel.

17 [*Duly sworn to by Harry H. Wiggins; jurat omitted in printing.*]

18 *Exhibit A to petition*

SN–N

TREASURY DEPARTMENT,
Washington, Mar. 7, 1938.

Office of Commissioner of Internal Revenue.

Mr. PAUL R. G. HORST,
% Duer, Strong & Whitehead,
15 Broad Street, New York, New York.

SIR: You are advised that the determination of your income tax liability for the taxable year(s) ended December 31, 1934, discloses a deficiency of $13,903.09 as shown in the statement attached.

In accordance with section 272 (a) of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT: C1: P-7. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
Commissioner,
By JOHN R. KIRK,
Deputy Commissioner.

Enclosures:
Statement.
Form 870.

19 STATEMENT

IT: A: 2.
MEK: 90D.

Mr. Paul R. G. Horst, % Duer, Strong & Whitehead, 15 Broad Street, New York, New York

Tax Liability for Taxable Year Ended December 31, 1934: Income tax, liability $37,710.22; assessed $23,807.13; deficiency $13,903.09.

The deficiency as shown herein results from including $25,182.50, representing the value of certain bond coupons detached and transferred to your son Robert P. K. Horst as a gift during the year 1934.

Adjustments to Net Income

Net income as shown in revenue agent's report dated July 6, 1936 (Deficiency arising from adjustments in revenue agent's report assessed in accordance with 870 agreement)	$92,544.73
Add: (a) Value of bond coupons transferred to Robert P. K. Horst	25,182.50
Net income adjusted	$117,727.23

Explanation of Adjustments

(a) The value of coupons transferred by you to your son is held to be taxable income to you for the reason that the bonds themselves had not been transferred to your son. I. T. 3011 Cumulative Bulletin XV-2 page 132 (1936) provides that interest

on bonds prior to a trust is income taxable to settlor and not to the beneficiaries, even though the settlor returns his income on the cash receipts and disbursements basis.

Computation of Tax

Net income adjusted		$117,727.23
Less: Personal exemption		2,500.00
Balance (surtax net income)		$115,227.23
Less:		
Dividends	$24,421.00	
Earned income credit ($3,000.00)	300.00	24,721.00
Balance subject to normal tax		$90,506.23
Normal tax at 4% on $90,506.23		$3,620.25
Surtax on $115,227.23		35,918.16
Total tax		$39,538.41
Less: Taxes paid to a foreign country		1,828.19
Tax liability		$37,710.22
Tax previously assessed:		
Original account #200174	$22,910.03	
Additional November 1936, account #510082	897.10	
		23,807.13
Deficiency of income tax		$13,903.09

21 Know all men by these presents: That I, Paul R. G. Horst, of 152 Carroll Street, Brooklyn, New York, have made, constituted, and appointed, and by these presents, do make, constitute, and appoint Selden Bacon of Pleasantville, New York, Marshal Stearns of New Canaan, Connecticut, Hugh Morgan, Jr., of West New Brighton, Richmond County, New York, Orwill V. W. Hawkins of Plandome, Nassau County, New York, and Harry H. Wiggins, of Little Neck, Nassau County, New York, any or all of them, to be my true and lawful attorneys for me and in my name, place, and stead to execute and file in my behalf amended returns, reports, claims for abatement, claims for refund, claims for credit, and any and all claims and other papers or documents, which may in any way affect or have any connection with any and all income-tax returns heretofore or hereafter filed by me and all income taxes at any time paid by me for the years covered by said returns or any additional income taxes claimed to be due under said income-tax returns or on account of income taxes covered by said returns, under the provisions of the Revenue Laws or other Statutes of the United States, and to appear for me before the Commissioner of Internal Revenue of the United States and any Board, Bureau, officers or other representatives of the Government of the United States or of any of its departments in connection with any of the aforesaid matters, and to attend conferences, prepare and submit briefs and make arguments in my behalf in connection therewith, to take appeals on my behalf to the United States Board of Tax Appeals relating to the aforesaid and sign the petition on said appeal, and any and all documents in any way connected with said appeal, and to appear before

said Board of Tax Appeals in my behalf, submit briefs, make arguments and do all and everything in any way connected or relating to such an appeal and to receive and collect refunds and reclaims arising out of any of the aforesaid matters.

For better and more effectually executing the powers and au-
22 thorities aforesaid, to do and perform all and every act and thing whatsoever requisite and necessary to be done in and about the premises as fully to all intents and purposes as I might or could do, if personally present at the doing thereof, with full power of substitution and revocation, hereby ratifying and confirming all that my said attorneys shall lawfully do or cause to be done by virtue hereof. This authority to remain in full force until revoked by me.

I hereby revoke the power of attorney given by me to William H. Van Benschoten, dated and acknowledged the 6th day of July 1926.

In witness whereof, I have hereunto set my hand and seal the 27 day of Aug. in the year of Our Lord, one thousand nine hundred and thirty.

PAUL R. G. HORST.

GERMAN REICH, STATE OF BAVARIA,
Consulate General of the United
States of America at Munich, ss:

Be it known, That on this 27th day of One thousand nine hundred and thirty, at the City of aforesaid, before me a Consul General of the United States of America, dwelling in said City of Munich, personally came and appeared Paul R. G. Horst, to me known, and known to me to be the individual described in, and who executed, the foregoing instrument, and he acknowledged to me that he executed the same.

In testimony whereof, I have hereunto set my hand and affixed the Consular Seal of the United States of America at the City of Munich aforesaid, the day and year last above written.

[CONSULAR SEAL] CHARLES M. HATHAWAY, Jr.,
Charles M. Hathaway, Jr.,
Consular General of the United States of America.

Fee No. 45. Service No. 2506. U. S. Gold. No fee.

23 Before United States Board of Tax Appeals

Docket No. 93220

[Title omitted.]

Answer

Filed May 20, 1938

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

I. Admits the allegations contained in Paragraph I of the petition.

II. Admits the allegations contained in Paragraph II of the petition.

III. Admits the allegations contained in Paragraph III of the petition.

IV. Denies that the respondent's determination is erroneous as alleged in Paragraph IV of the petition.

V. Admits the allegations of fact contained in Paragraph V of the petition.

VI. Denies generally and specifically each and every allegation contained in the petition and not hereinbefore admitted, qualified, or denied.

24 Wherefore, it is prayed that the appeal be denied.

(Signed) J. P. WENCHEL,
G. W. K.
J. P. Wenchel,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:
CHESTER A. GWINN,
ARTHUR W. CARNDUFF,
Special Attorneys,
Bureau of Internal Revenue.

Before United States Board of Tax Appeals

PAUL R. G. HORST, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket Nos. 90819, 93220. Promulgated April 12, 1938.

Findings of fact and opinion

The owner of foreign, state, municipal, and industrial coupon bonds, clipped therefrom and delivered before maturity to another, as a gift, negotiable interest coupons having a maturity within the taxable year. Payments were received on the coupons by the donee within the taxable year. The donor was the owner of the bonds throughout the taxable year and kept his books and made his income-tax returns on the cash receipts and disbursements basis. Held, that the amounts received by the donee on the coupons were taxable income to the donor.

25 Harry H. Wiggins, Esq., for the petitioner.
J. R. Johnston, Esq., for the respondent.

These consolidated proceedings involve the redetermination of income tax deficiencies in the amounts of $13,903.09 and $12,376.20 for the respective years 1934 and 1935.

The facts are all stipulated and we adopt the stipulation as our findings of fact. For the purposes of our opinion we deem it necessary to set forth herein only the following findings of fact.

Findings of fact

1. Petitioner is and was during the years 1934 and 1935 a citizen of the United States, temporarily residing at No. 3 Avenue Elisee Reclus, Paris, France.

2. During the years 1934 and 1935 petitioner kept his books and made his income tax returns on the cash receipts and disbursements basis.

3. Throughout the year 1934 petitioner owned foreign state, municipal, and industrial coupon bonds from which, on the 10th day of August 1934, he detached and transferred by manual delivery to his son, Robert P. K. Horst, as a gift, prior to their maturity, negotiable interest coupons of an aggregate face value of $25,182.50.

4. All of such coupons matured during the year 1934 and in that year Robert P. K. Horst collected therefrom the total amount of $25,182.50 and reported such amount in his Federal income tax return for that year.

5. Throughout the year 1935 petitioner owned foreign state, municipal, and industrial coupon bonds from which, in August 1935, he detached and transferred by manual delivery to his son, Robert P. K. Horst, as a gift, prior to their maturity, negotiable interest coupons of an aggregate face value of $37,032.50.

26 6. All of such coupons matured during the year 1935 and in that year Robert P. K. Horst collected therefrom the total amount of $25,495 and reported such amount in his Federal income tax return for that year.

7. Petitioner did not report in his income tax return for the year 1934 any part of the amount represented by the interest coupons delivered as a gift to his son in that year, and petitioner did not report in his income tax return for the year 1935 any part of the amount represented by the interest coupons delivered as a gift to his son in that year.

8. Repondent in determining the deficiency for the year 1934 added to the taxable income of the petitioner the amount of $25,182.50 as the value of the coupons transferred to Robert P. K. Horst in that year, and in determining the deficiency for the year 1935, respondent added to the taxable income of the petitioner the sum of $22,360 as the aggregate net worth of all of the coupons transferred by petitioner to his son in that year.

9. Deficiency in income tax for the year 1934 resulted solely from the addition to income of petitioner in that year of the above stated amount of $25,182.50. The deficiency in income tax for the year 1935 resulted from the addition to income of petitioner in that year of the above-stated amount of $22,360 plus certain other minor adjustments not in controversy here.

Opinion

HILL: There is only one question for determination, namely, whether the amounts collected in the respective years 1934 and 1935 on the coupons involved are taxable as income to petitioner. We think they are. It is true that we were reversed on a similar point in our decision in Julius Rosenwald, 12 B. T. A. 350, by the United States Circuit Court of Appeals for the Seventh Circuit, 33
27 Fed. (2d) 423. The court assigned as the basis for such reversal that the severance and delivery of the coupons before maturity constituted a completed gift and hence the coupons were not taxable to the owners of the bonds from which they had been severed. We think our decision in that case was right and respectfully decline to follow the decision of the Circuit Court of Appeals on the point stated. Unquestionably the gift of the coupons in that case, as well as in the instant case, was a completed one, but it was, nevertheless, a gift of income. The severance and negotiation of an interest coupon does not change the character of the thing which it evidences and represents. That thing is interest on the bond from which the coupon was severed. Such interest is income derived from the bond, whether it be paid to the owner of the bond or to his donee or assignee. The owner of property which produces income is chargeable with such income for tax purposes regardless of whether he receives or enjoys the income. Van Meter v. Commissioner, 61 Fed. (2d) 817; Bing v. Bowers, 22 Fed. (2d) 450; affirmed per curiam (C. C. A., 2d Cir.), 26 Fed. (2d) 1017; Ward v. Commissioner (C. C. A., 9th Cir.), 58 Fed. (2d) 757.

In the Van Meter case, supra, the court said:

"The Supreme Court has definitely determined that Congress has the power to tax the earner of income, therefore, irrespective of whether it is paid to someone else. [Citing a number of cases.]

"The 'earner' of income is one whose personal efforts have produced it; who owns property which produced it or a combination of the two. Decisions of the Supreme Court have declared that the income statutes require taxation to the earner in each of the three above sources of income where the income was actually realized but never came to beneficial enjoyment by the earner. * * *

"In determining who is taxable for an income, there are three
28 considerations which may be of importance, to wit, who earns the income, who receives it, and who enjoys it. Where the same person earns, receives, and enjoys the income (the normal and usual situation), there is no difficulty. Where different persons earn, receive, and/or enjoy the income, disputes occur. In determining such disputes, the vital matter is always the relation of the earner (whether a person, owner of property or combination of the two) of the income to the income so earned. The rule and intent of the taxing statutes is that the earner of income which he might and, normally, would receive and enjoy for himself is not relieved because he chooses not to receive or not to enjoy it, and this is not necessarily changed by

such deprivation taking the form of an obligation legally binding him thereto, * * * but where the earner of the income does nothing more than transfer the income earned in his own right to another, even though such disposal be in advance of the earning thereof (Burnet v. Leininger and Lucas v. Earl, supra), or where he retains any power of control over the income earning property or the income therefrom (Corliss v. Bowers, 281 U. S. 376, 50 S. Ct. 336, 74 L. Ed. 916, and analogous as to transfer tax, Chase Nat. Bank v. U. S., 278 U. S. 327, 49 S. Ct. 126, 73 L. Ed. 405, 63 A. L. R. 388; Reinecke v. Northern Trust Co., 278 U. S. 339, 49 S. Ct. 123, 73 L. Ed. 410, 66 A. L. R. 397, and as to State succession tax, Saltonstall v. Saltonstall, 276 U. S. 260, 48 S. Ct. 225, L. Ed. 565), such income is taxable to him within the intent of the statute (Burnet v. Leininger, Lucas v. Earl and Corliss v. Bowers, supra).

"* * * It may be true that income already entirely earned is transferable as a species of property, but that has no effect upon the power and intention of Congress to tax income to the earner. The earner may, in a legally binding way, dispose of his earnings, whether they are already earned or are to be earned, without affecting in the slightest manner his status as earner thereof and his resulting liability for taxation thereon as income."

In the case of Bing v. Bowers, supra, the court said:

"To permit the assignor of future income from his own property to escape taxation thereon by a gift grant in advance of the receipt by him of such income would by indirection enlarge the limited class of deductions established by statute. As long as he remains the owner of the property, the income therefrom should be taxable to him as fully, when he grants it as a gift in advance of its receipt, as it clearly is despite a gift thereof immediately after its receipt."

The Ward case, supra, affirming 22 B. T. A. 352, supports the proposition that the owner of income producing property is chargeable, for tax purposes, with the income therefrom even though he may have transferred such income by gift or other assignment to another. The court, in the Ward case, quoted with approval from Rosenwald v. Commissioner (C. C. A. 7th Cir.), 33 Fed. (2d) 423, 426, as follows:

"Petitioner's chief contention is that there was a completed gift, and that petitioner never received the income.

"It is doubtful whether a holder of securities may separate the income thereafter to accrue from the principal, and make a gift by way of assignment of the income, without assigning or trusteeing the thing out of which the income arises, where the effect would be to relieve the donor from a tax he would otherwise be required to pay."

The court, in the Ward case, further said:

"Numerous other cases also hold that assigned income is taxable to the assignor, unless the corpus producing the income is also assigned." See Appeal of Fred W. Warner, 5 B. T. A. 963, and Irene McFadden Winder, Executrix, v. Commissioner, 17 B. T. A. 303, and cases cited therein. See, also, Porter v. United States (Ct.

Cl.), 52 Fed. (2d) 1056; Bishop v. Commissioner (C. C. A., 7), 54 Fed. (2d) 298.

Petitioner contends that he is not taxable on the items here involved for the reason that the coupons in question when severed and negotiated before maturity of the interest they represented became separate and independent instruments. Conceding that upon severance the coupons became separate and independent instruments, the fact remains that the proceeds of the coupons when collected constituted income derived from the bonds from which they were severed. It is stipulated that the ownership of the bonds remained at all times during the taxable years in petitioner.

The facts in the instant case clearly distinguish it from the case of Rebekah C. Schoonmaker, 39 B. T. A. — (Feb. 24, 1939). In the latter case the gift was of bonds with unmatured interest coupons attached. In other words, the gift in that case was of income producing property, the income from which for the taxable year had not at the time of the gift been received, either actually or constructively, by the donor, whose books and income tax returns were on the cash receipts and disbursements basis. We held in that case that the accrued but unmatured interest represented by the interest coupons was not includable as taxable income to the donor. In the instant case the income producing property was retained by the donor and only the accruing income therefrom in the taxable years was transferred as a gift to another prior to the time of its maturity.

We hold that petitioner is chargeable with income, for tax purposes, in the full amounts collected from the coupons in question in the respective years 1934 and 1935. However, respondent based his determination of deficiency for the year 1935 on the addition to petitioner's income in such year of only $22,360, instead of $25,495, the amount actually collected from the coupons in that year, and has not asked for an increased deficiency. Accordingly, we approve the respondent's determinations.

31

Reviewed by the Board.

Decision will be entered for the respondent.

BLACK, dissenting: When negotiable coupons attached to coupon bonds are detached it seems to me they become separate and distinct property from the bonds and are subject to be sold separately or to be the subject of a completed gift, inter vivos. If a gift of such detached coupons is made by the owner prior to their maturity there would be no realization of income thereby to the donor. Cf. Rebekah C. Schoonmaker, 39 B. T. A. — (Feb. 24, 1939). There would likewise be no income to the donee by reason of the gift itself. See section 22 (b) (3) of the Revenue Act of 1934, which reads:

"(b) Exclusions from Gross Income.—The following items shall not be included in gross income and shall be exempt from taxation under this title:

"(3) Gifts, Bequests, and Devices.—The value of property acquired by gift, bequest, devise, or inheritance (but the income from such property shall be included in gross income)."

However, when the coupons matured in the hands of the donee and he collected them the amount collected was income to him as interest. See section 22 (a) of the Revenue Act of 1934. The entire amount collected, even if it be not proper to call all of it
32 interest, would be income to the donee, if the coupons had no cost basis to the donor, as indeed in most cases they would not have unless the donor purchased the bonds with some accrued but unmatured interest coupons attached. The donee has the same basis of cost as the donor. See section 113 (a) (2) of the Revenue Act of 1934.

The findings of fact in the majority opinion show that in each of the taxable years Robert P. K. Horst, the donee of the unmatured coupons, collected the interest due thereon when it matured and returned the entire amount for taxation in the year the interest was collected. This, I think, was proper because the coupons had no cost basis to the donor and hence none to the donee.

I think the court was right in holding in Rosenwald v. Commissioner, 33 Fed. (2d) 423, that Rosenwald's delivery to a charitable fund of negotiable Third Liberty Loan bond coupons before their maturity constituted a completed gift and the interest thereafter collected by the charitable fund from such bond coupons was not income to the donor. The evidence upon which the court based its decision in the Rosenwald case as to the Liberty bond coupons is stated in the court's opinion as follows: "There is evidence that petitioner clipped and delivered to the fund, before their maturity, interest coupons from Third Liberty Loan Bonds."

The facts in the instant case seem clearly to bring it within the rule announced by the court in the Rosenwald case. I, therefore, respectfully dissent from the majority opinion.

LEECH and DISNEY agree with this dissent.

33 Before United States Board of Tax Appeals, Washington

Docket Nos. 90819, 93220

PAUL R. G. HORST, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Pursuant to the determination of the Board, as set forth in its findings of Fact and Opinion, promulgated April 12, 1939, it is

Ordered and decided: That there are deficiencies in income tax for the years 1934 and 1935, in the amounts of $13,903.09 and $12,376.20, respectively.

Enter:

Entered April 17, 1939.

(Signed) SAM B. HILL, *Member.*

34 Before United States Board of Tax Appeals

Docket Nos. 90819, 93220

[Title omitted.]

Petition for review and assignments of error

Filed June 30, 1939

The above-named petitioner hereby petitions for a review by the United States Circuit Court of Appeals for the Second Circuit of the decision of the United States Board of Tax Appeals rendered on the 17th day of April, 1939, 39 B. T. A., No. 102, determining deficiencies in the petitioner's Federal income taxes for the calendar years 1934 and 1935 in the respective amounts of $13,903.09 and $12,376.20; and respectfully shows:

I. That the petitioner is and was during the years 1934 and 1935 a citizen of the United States, temporarily residing at No. 3 Avenue Elisee Reclus, Paris, France, and filed his income-tax returns for the calendar years 1934 and 1935, which are the taxable years involved herein, with the Collector of Internal Revenue for the First District of New York, whose office is located in the County of Kings, in the State of New York, and within the territorial jurisdiction of the United States Circuit Court of Appeals for the Second Circuit.

II. The controversy involves the petitioner's liability for Federal income taxes for the calendar years 1934 and 1935.

35 The petitioner, on August 10, 1934, detached from certain foreign, state, municipal and industrial coupon bonds owned by him, and transferred by manual delivery to his son, Robert P. K. Horst, as a gift, prior to their maturity, negotiable interest coupons of an aggregate face value of $25,182.50. The said Robert P. K. Horst, in the year 1934, collected from the said coupons, at their maturity, the total amount of $25,182.50, and reported said amount in his Federal income tax return for that year.

The petitioner, in August, 1935, detached from certain foreign, state, municipal and industrial coupon bonds owned by him, and transferred by manual delivery to his son, Robert P. K. Horst, as a gift, prior to their maturity, negotiable interest coupons of an aggregate face value of $37,032.50. The said Robert P. K. Horst, in the year 1935, collected from the said coupons, at their maturity, the total amount of $25,495.00, and reported said amount in his Federal income tax return for that year.

The petitioner did not report any part of the amount represented by the interest coupons delivered as a gift to his son in the year 1934, in his income tax return for that year, nor any part of the amount represented by the interest coupons delivered as a gift to his son in the year 1935, in his income tax return for that year.

The Commissioner of Internal Revenue, the respondent herein, held that the amounts collected by the petitioner's son from the coupons delivered in the respective years 1934 and 1935, prior to their

aturity, by the petitioner to his son, as a gift, were taxable as income o the petitioner; and the Commissioner added to the petitioner's ncome the amounts of $25,182.50 and $22,360.00 for the years 1934 nd 1935, respectively, and determined deficiencies in the petitioner's ncome tax for the years 1934 and 1935 in the amounts of $13,903.09 nd $12,376.20, respectively.

The United States Board of Tax Appeals approved the Commisioner's determination.

III. The petitioner, being aggrieved by the determination 36 of the United States Board of Tax Appeals as set forth in its findings of fact and opinion, promulgated April 22, 1939, and by ts decision rendered pursuant thereto desires to obtain a review thereof by the United States Circuit Court of Appeals for the Second Circuit.

IV. The petitioner, as a basis for review, makes the following assignments of error:

1. The United States Board of Tax Appeals erred in holding that the amount collected by the petitioner's son from the coupons delivered on August 10, 1934, prior to their maturity, by the petitioner to his son, as a gift, was taxable income to the petitioner.

2. The United States Board of Tax Appeals erred in including in the petitioner's income for 1934 the sum of $25,182.50, representing the amount collected by the petitioner's son from negotiable interest coupons detached from certain foreign, state, municipal and industrial coupon bonds owned by the petitioner, and transferred by manual delivery, prior to maturity, by the petitioner to his son, Robert P. K. Horst, as a gift.

3. The United States Board of Tax Appeals erred in holding that the amount collected by the petitioner's son from the coupons delivered in August 1935, prior to their maturity, by the petitioner to his son, as a gift, was taxable as income to the petitioner.

4. The United States Board of Tax Appeals erred in including in the petitioner's income for 1934 the sum of $25,182.50, representing the amount collected by the petitioner's son from negotiable interest coupons detached from certain foreign, state, municipal and industrial coupon bonds owned by the petitioner, and transferred by manual delivery, prior to maturity, by the petitioner to his son, Robert P. K. Horst, as a gift.

37 5. The United States Board of Tax Appeals erred in determining deficiencies in the petitioner's income tax for the years 1934 and 1935 instead of determining that there is no deficiency due from the petitioner for the year 1934 and that there is an overpayment of income tax of $1,730.33 for the year 1935.

HARRY H. WIGGINS,
Harry H. Wiggins,
Attorney for Petitioner.

Office & P. O. Address, No. 15 Broad Street, Borough of Manhattan, New York City, N. Y.

[*Duly sworn to by Harry H. Wiggins; jurat omitted in printing.*]

38 Before United States Board of Tax Appeals

Docket Nos. 90819 and 93220

[Title omitted.]

Notice of filing petition for review

Filed July 13, 1939

To J. P. WENCHEL, *Esq.*,
Chief Counsel, Bureau of Internal Revenue, Washington, D. C.

SIR: Please take notice that the petitioner did on the 30th day of June 1939 file with the Clerk of the United States Board of Tax Appeals at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit of the decision of the Board heretofore rendered in the above-entitled appeals. A copy of the petition for review and the assignments of error as filed is hereto attached and served on you.

Dated New York, N. Y., July 7, 1939.

Respectfully,

HARRY H. WIGGINS,
Harry H. Wiggins,
Attorney for Petitioner.

Office and Post Office Address, No. 15 Broad Street, Borough of Manhattan, New York City.

39 Personal service of the foregoing notice, together with a copy of the Petition for Review and Assignments of Error mentioned therein is hereby acknowledged this 8th day of July 1939.

J. P. WENCHEL,
W.
Chief Counsel, Bureau of Internal Revenue,
Attorney for Respondent.

Before United States Board of Tax Appeals

Docket No. 90819

[Title omitted.]

Stipulation of facts

Filed at Hearing, Jan. 9, 1939

It is hereby stipulated and agreed by and between the parties hereto, through their respective counsel of record, that the following facts shall be taken as true, provided however that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent with the facts herein stipulated to be true.

1. That the petitioner is and was during the year 1935 a
40 citizen of the United States, temporarily residing at No. 3 Avenue Elisee Recius, Paris, France.

2. That on the dates hereinafter set out, the petitioner detached, transferred, and delivered to his son, Robert P. K. Horst, as a gift, prior to their maturity, the following described negotiable interest coupons from the following-described bonds of which the petitioner was the owner throughout the year 1935, to wit:

Principal amount of bond	Name of bond	Due date of coupon	Face amount of coupon	Amount collected	Date of gift
101M	City of Milan, Italy 6½–52	10-1-35	$3,282.50	$3,282.50	8-21-35
100M	City of Rome, Italy 6½–52	10-1-35	3,250.00	3,250.00	8-21-35
100M	City of Tokyo, Japan 5½–52	10-1-35	2,750.00	2,750.00	8-24-35
100M	City of Yokohama, Japan 6–61	12-1-35	3,000.00	3,000.00	8-24-35
200M	Kingdom of Italy 7–51	12-1-35	7,000.00	7,000.00	8-24-35
200M	U. S. of Brazil 8–41	12-2-35	8,000.00	2,800.00	8-21-35
70M	U. S. of Brazil 6½–57	10-15-35	2,275.00	796.25	8-21-35
230M	U. S. of Brazil 6½–57	10-1-35	7,475.00	2,616.25	8-21-35
			37,982.50	25,495.00	

3. The Commissioner in determining the deficiency for the year 1935, added to the taxable income of the petitioner, the sum of $22,360.00 as the aggregate net worth of all of the above coupons at the time of transfer by him to his son.

4. For the year 1935, the said Robert P. K. Horst collected from the above-described coupons, at their maturity, the respective amounts shown by the statement in Paragraph 2 hereof, and in the sum of $25,495.00.

41 5. For the year 1935, the petitioner kept his books and made his return of income to the Federal Government on the cash receipts and disbursements basis.

6. That the pleadings shall be deemed amended, if necessary, to conform to the facts set forth in this stipulation.

HARRY H. WIGGINS,
Counsel for Petitioner.
J. P. WENCHEL,
J. P. Wenchel,
Chief Counsel,
Bureau of Internal Revenue.

Before United States Board of Tax Appeals

Docket No. 93220

[Title omitted.]

Stipulation of facts

Filed at Hearing, Jan. 9, 1939

It is hereby stipulated and agreed by and between the parties hereto, through their respective counsel of record, that the following facts shall be taken as true, provided however that this stipulation

shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent with the facts herein stipulated to be true.

42 1. That the petitioner is and was during the year 1934 a citizen of the United States, temporarily residing at No. 3 Avenue Elisee Reclus, Paris, France.

2. That on the 10th day of August, 1934, the petitioner detached and transferred by manual delivery to his son, Robert P. K. Horst, as a gift, prior to their maturity, the following described negotiable interest coupons of an aggregate face value of $25,182.50 from the following-described bonds owned by petitioner throughout the year 1934, to wit:

Face value of coupons	Name of bond	Due date of coupons (1934)	Date of gift (1934)
$3,500.00	Toho Electric Power Co. 7s due 1955	Sept. 15	Aug. 10
$3,507.00	Ujigawa Electric Power Co. 7s due 1945	Sept. 15	Aug. 10
$3,282.50	City of Milan 6½s due 1952	Oct. 1	Aug. 10
$3,250.00	City of Rome 6½s due 1952	Oct. 1	Aug. 10
$2,750.00	City of Tokio 5½s due 1961	Oct. 1	Aug. 10
$3,000.00	City of Yokohama 6s due 1961	Dec. 1	Aug. 10
$4,500.00	Tokio Electric Light Co. 6s due 1953	Dec. 15	Aug. 10
$1,400.00	Kingdom of Italy 7s due 1951	Dec. 1	Aug. 10

3. That during the year 1934, the said Robert P. K. Horst collected the said coupons and reported the collections therefrom in the sum of $25,182.50 in his Federal income-tax return for that year.

4. That during the year 1934, the petitioner kept his books and made his return of income on the cash receipts and disbursements basis.

43 5. That the pleadings shall be deemed amended, if necessary, to conform to the facts set forth in this stipulation.

HARRY H. WIGGINS,
Counsel for Petitioner.
J. P. WENCHEL,
J. P. Wenchel,
Chief Counsel, Bureau of Internal Revenue.
Counsel for Respondent.

Before United States Board of Tax Appeals

Docket Nos. 90819 and 93220

[Title omitted.]

Praecipe for record

Filed July 13, 1939

To the CLERK OF THE UNITED STATES BOARD OF TAX APPEALS:

You are hereby requested to prepare and certify and transmit to the Clerk of the United States Circuit Court of Appeals for the Second Circuit, with reference to the Petition for Review heretofore filed by

he Petitioner in the above entitled appeals, a transcript of the record n the above-entitled appeals, prepared and transmitted as required y law and by the rules of said Court, and to include in said transcript f record the following documents, or certified copies thereof, to wit,

4 1. The docket entries of all proceedings before the Board of Tax Appeals in the above-entitled appeals.

2. The pleadings before the Board of Tax Appeals in Docket No. 0819, as follows:

(a) Petition for Redetermination,

(b) Answer of the Respondent,

3. The pleadings before the Board of Tax Appeals in Docket No. 3220, as follows:

(a) Petition for Redetermination,

(b) Answer of the Respondent,

4. The Findings of Fact and Opinion of the Board of Tax Appeals.

5. The Decision of the Board.

6. The Petition for Review filed by the Petitioner in the above-entitled appeals, together with notice of filing thereof and admissio of service endorsed thereon.

7. Stipulation of Facts in Docket No. 90819.

8. Stipulation of Facts in Docket No. 93220.

9. This Praecipe.

Yours, etc.,

HARRY H. WIGGINS,
Harry H. Wiggins,
Attorney for Petitioner.

Office and Post Office Address: No. 15 Broad Street, Borough of Manhattan, New York City.

5 Personal service of a copy of the foregoing Praecipe is hereby acknowledged this 8th day of July, 1939.

J. P. WENCHEL,
W.
Chief Counsel, Bureau of Internal Revenue,
Attorney for Respondent.

[Clerk's certificate to foregoing transcript omitted in printing.]

46 In United States Circuit Court of Appeals for the Second Circuit

No. 83—October Term, 1939

(Argued October 18, 1939—Decided November 13, 1939)

PAUL R. G. HORST, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal from the Board of Tax Appeals

Petition by Paul R. G. Horst to review a decision of the Board of Tax Appeals, determining deficiencies in income tax for 1934 and 1935. Reversed.

Before SWAN, CHASE, and PATTERSON, Circuit Judges.

Duer, Strong & Whitehead (Orville V. W. Hawkins and Harry H. Wiggins, of counsel), for petitioner. Samuel O. Clarke, Jr., Assistant Attorney General, and Sewall Key and Morton K. Rothschild, Special Assistants to the Attorney General, for respondent.

47 *Opinion*

PATTERSON, Circuit Judge:

The question is whether a taxpayer who detaches coupons from bonds owned by him and delivers them to another as a gift prior to the time when the coupons are payable is liable for income tax on the amounts later collected on the coupons by the transferee.

The petitioner owned a number of coupon bonds. The coupons represented the interest on the bonds and were payable to bearer. In 1934 he detached unmatured coupons of face value of $25,182.50 and transferred them by manual delivery to his son as a gift. The coupons matured later on in the same year, and the son collected the face amount, $25,182.50, as his own property. There was a similar transaction in 1935. The petitioner kept his books on a cash basis. He did not include any part of the moneys collected on the coupons in his income tax returns for these two years. The son included them in his returns. The Commissioner added the moneys collected on the coupons to the petitioner's taxable income and determined a tax deficiency for each year. The Board of Tax Appeals, three members dissenting, sustained the Commissioner, holding that the amounts collected on the coupons were taxable as income to the petitioner.

The Board refused to follow Rosenwald v. Commissioner, 33 F. 2d, 423 (C. C. A. 7), certiorari denied, 280 U. S. 599, where the facts were the same as in the present case. Rosenwald clipped bearer

coupons and delivered them to a donee prior to the due date. The donee collected the money due. It was held that the interest collected on the coupons was not income of Rosenwald for tax purposes. The Board's decision is also in substance contrary to Matchette v. Helvering, 81 F. 2d, 73 (C. C. A. 2), where we held that a stockholder who made an outright assignment of a dividend to another after declaration but before time of payment was not obliged to include the dividend in his income. We are of opinion that those
48 decisions were sound and that the Board's decision cannot stand.

When the petitioner detached the coupons and handed them over to his son as a gift, the son acquired full title and dominion. The petitioner could not interfere in any way with the donee's control and right to receive the money when the coupons matured. Taxwise, the transaction was an outright assignment of future income from property, with the assignee the owner of the income prior to and at its realization. Generally liability to income tax attaches to ownership of the income, Blair v. Commissioner, 300 U. S. 5, and we see nothing to take the case out of the general rule. The case is not one where the assignor had power over the income after the assignment, as in Corliss v. Bowers, 281 U. S. 376. Nor is it a case of assignment of future earnings, the effectiveness of which for practical purposes is dependent on continued performance of services by the assignor. See Lowery v. Helvering, 70 F. 2d, 713 (C. C. A. 2); Rossmoore v. Commissioner, 76 F. 2d, 520 (C. C. A. 2); Shanley v. Bowers, 81 F. 2d, 13 (C. C. A. 2); Matchette v. Helvering, supra.

The Board thought that a person who assigns future income from property and retains the property producing the income is liable for income tax on the income belonging to the transferee. The proposition, stated as broadly as this, cannot be supported. Take a case where the owner of income-producing property, such as bonds or stocks, grants by formal instrument a life estate in the property to another, keeping no power of revocation or control during the life estate but reserving the reversionary interest. The life estate is essentially a transfer of future income for the grantee's life; the corpus stays with the grantor. It would hardly be contended that in such a case the grantor was liable for income tax on the income belonging to the life tenant unconditionally. The situation may be varied by supposing that the estate created was one for
49 years rather than for life, without affecting the result. See United States v. First National Bank, 74 F. 2d, 360 (C. C. A. 5).

The respondent relies on Lucas v. Earl, 281 U. S. 111, and Burnet v. Leininger, 285 U. S. 136. We do not see that these cases support the Board's decision. In Lucas v. Earl, a husband assigned to his wife salaries and fees to be earned in the future. The salaries and fees later earned by him were held to be taxable income to him. In Burnet v. Leininger, a partner assigned to his wife future income from the partnership. The partner was nevertheless held liable for

income tax on such income. It is true that these two cases were given a broad interpretation in Reinecke v. Smith, 289 U. S. 172, 177; but in a more recent case, Blair v. Commissioner, supra, it was pointed out that they concerned assignments of future income from earnings, that they were decided on the provisions of the revenue act applicable to income derived from personal services and from partnerships, and that they did not control assignments of future income from property.

The Board quotes a passage from Bing v. Bowers, 22 F. 2d, 450, affirmed on the opinion below in 26 F. 2d, 1017 (C. C. A. 2). The language quoted must be read against the facts of that case, where it was held that the taxpayer had given up no interest in the land, had created no rent charge, and had in fact retained control over the net income which he had purported to grant to another.

The amounts collected on the coupons were not income of the petitioner. The decision of the Board will be reversed.

50 In United States Circuit Court of Appeals, Second Circuit

PAUL R. G. HORST, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal From the United States Board of Tax Appeals

Judgment

Filed Dec. 2, 1939

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the order of said United States Board of Tax Appeals be and it hereby is reversed.

It is further ordered that a Mandate issue to the said Board in accordance with this decree.

D. E. ROBERTS, *Clerk.*

51 [File endorsement omitted.]

52 [Clerk's certificate to foregoing transcript omitted in printing.]

53 Supreme Court of the United States

Order allowing certiorari

Filed April 8, 1940

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsement on cover:] File No. 44190. U. S. Circuit Court of Appeals, Second Circuit. Term No. 27. Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, vs. Paul R. G. Horst. Petition for a writ of certiorari and exhibit thereto. Filed March 2, 1940. Term No. 27 O. T. 1940.

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In the Supreme Court of the United States

OCTOBER TERM, 1939

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

PAUL R. G. HORST

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit entered in the above-entitled cause on December 2, 1939, reversing the decision of the United States Board of Tax Appeals.

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 24) is reported in 39 B. T. A. 757. The opinion of the Circuit Court of Appeals (R. 46) is reported in 107 F. (2d) 906.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 2, 1939 (R. 49). The

jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the owner of coupon bonds should include in his gross income the amount of coupons which he detached and gave to his son several months prior to maturity.

STATUTE INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived * * * from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * * [U. S. C., Title 26, Sec. 22].

STATEMENT

The stipulation of facts (R. 39–43) was adopted by the Board of Tax Appeals as its findings of fact; they are substantially as follows (R. 25–26):

Taxpayer is and was during the years 1934 and 1935 a citizen of the United States, temporarily residing in Paris, France (R. 25).

During the years 1934 and 1935 taxpayer kept his books and made his income-tax returns on the cash receipts and disbursements basis (R. 25).

Throughout the year 1934 taxpayer owned foreign, state, municipal, and industrial coupon bonds. On August 10, 1934, he detached, prior to their maturity, negotiable interest coupons and transferred them by manual delivery to his son, Robert P. K. Horst, as a gift. They had an aggregate face value of $25,182.50. (R. 25.) All of the coupons matured during the year 1934; and in that year the son collected the total amount due and reported it in his income-tax return for that year (R. 25).

Throughout the year 1935 taxpayer owned foreign, state, municipal, and industrial coupon bonds. In August 1935 he detached, prior to their maturity, negotiable interest coupons and transferred them by manual delivery to his son as a gift. They had an aggregate face value of $37,032.50. (R. 25.) All of the coupons matured during the year 1935, and in that year the son collected the amount of $25,495 and reported it in his income-tax return for that year (R. 26).

The taxpayer did not report in his income-tax returns for the years 1934 and 1935 any part of the amount represented by the interest coupons delivered as a gift to his son in those years (R. 26). The Commissioner in determining the deficiency for the year 1934 added to the taxable income of the taxpayer the amount of $25,182.50 as the value of the coupons transferred to his son in that year, and in determining the deficiency for the year 1935 the Commissioner added to the taxable

income of the taxpayer the amount of $22,360 as the aggregate net worth of all of the coupons transferred by taxpayer to his son in that year (R. 26). The deficiency in income tax for the year 1934 resulted solely from the addition to income of the ~~value as set here. (R. 26.)~~ transferred coupons. The deficiency for the year 1935 resulted from the addition to income of the value of the transferred coupons plus certain other minor adjustments not in controversy here (R. 26).

The Board of Tax Appeals upheld the Commissioner's determination, with three members dissenting, and the taxpayer appealed to the Circuit Court of Appeals, which reversed the Board's decision and held that the amount of the coupons was not income of the taxpayer.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the owner of bonds need not include the amount of certain coupons in his gross income where he detached and gave the coupons to his son several months prior to maturity.

2. In failing to hold that the owner of bonds should include the amount of certain coupons in his gross income although he detached and gave the coupons to his son several months prior to maturity.

3. In reversing the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below conflicts in principle with decisions of this Court and of the circuit courts of appeals.

In *Helvering* v. *Clifford,* No. 383, this Term, decided February 26, 1940, this Court held the grantor of an irrevocable but short term trust taxable upon the income payable to the beneficiary. The issue, the Court said, was simply "whether the grantor after the trust has been established may still be treated, under this statutory scheme, as the owner of the corpus" (p. 3). The short period before reversion, and the retention of control over the principal, fortified by the familial relations between settlor and beneficiary, provided the solution to that issue. The result in the present case should follow *a fortiori* from the *Clifford* decision. For here the taxpayer has surrendered simply his claim to future income and has retained intact the entire bundle of rights which constitute his ownership of the underlying property.[1]

The decision below is not only in conflict with the *Clifford* case, but the court below has ignored the settled rule relating to the assignor's taxability upon assigned future income. *Lucas* v. *Earl,* 281 U. S. 111, in which the rule was first established,

[1] There can be no question that the coupons represented interest, divorced from the principal. *Old Colony R. Co.* v. *Commissioner,* 284 U. S. 552, 561; see *Deputy* v. *duPont,* No. 151, this Term, decided January 8, 1940.

dealt, it is true, with the income from personal services. But the basis of the decision is the broad principle that tax liability remains the same whether the income is assigned before or after its receipt; in this doctrine there is no room for distinction according as the future income is derived from the taxpayer's services or his ownership. Thus, in *Burnet* v. *Leininger,* 285 U. S. 136, the assignor was held taxable when the income, derived from a laundry partnership, was produced by a combination of property and personal services. And in *Reinecke* v. *Smith,* 289 U. S. 172, 177, the Court noted that "This court has repeatedly said that such an assignment, where the assignor continued to own the corpus, does not immunize him from taxation upon the income." See also *Saenger* v. *Commissioner,* 69 F. (2d) 631, 632 (C. C. A. 5th). With minor exceptions,[2] the circuit courts of appeals have consistently held that unless the taxpayer assigns the corpus which produces the income, he cannot by assignment of future income be relieved of taxation on that income. *Bing* v.

[2] In *Rosenwald* v. *Commissioner*, 33 F. (2d) 423, certiorari denied, 280 U. S. 599, the amount of income in dispute was about $830,000, of which about $815,000 represented assigned income from rents, stocks, and bonds, while $15,000 represented income from bond coupons assigned by the owner of the bonds. The court held the owner taxable on all except the coupons. The Government did not apply for a writ of certiorari in regard to the assigned coupons because of the relatively small amount of tax involved. Cf. *Matchette* v. *Helvering*, 81 F. (2d) 73 (C. C. A. 2d), certiorari denied, 298 U. S. 677.

Bowers, 22 F. (2d) 450, 454 (S. D. N. Y.) affirmed, 26 F. (2d) 1017 (C. C. A. 2d); *Rosenwald* v. *Commissioner,* 33 F. (2d) 423, 426 (C. C. A. 7th), certiorari denied, 280 U. S. 599; *Porter* v. *United States,* 52 F. (2d) 1056 (C. Cls.); *Ward* v. *Commissioner,* 58 F. (2d) 757 (C. C. A. 9th), certiorari denied, 287 U. S. 656; *Dickey* v. *Burnet,* 56 F. (2d) 917, 921 (C. C. A. 8th), certiorari denied, 287 U. S. 606; *Wood* v. *Commissioner,* 74 F. (2d) 78 (C. C. A. 6th).[3]

The substance of the transaction is, in truth, simply a gift by respondent of his income to his son. He clearly would be taxable on the amount of the bond coupons if he had collected the interest payments before giving the proceeds to his son; or, indeed, if he had directed the son to collect the coupons as his agent and to keep the proceeds as a gift.[4] These technical variations upon the transaction would not alter its practical substance, and respondent is taxable in this case equally with its

[3] See also 2 Paul & Mertens, *Law of Federal Income Taxation* (1934), Sec. 15.03, p. 25. A case substantially similar to this is now pending decision in the Supreme Judicial Court of Massachusetts. *Williston* v. *Commissioner of Corporations and Taxation,* Nos. 9063–9064.

[4] Indeed, under ordinary standards, the respondent made a gift to his son which was largely past rather than future income. The coupons were given one to four months in advance of maturity (R. 5, 16, 40, 42). Although respondent kept his books upon a cash basis, the commercial truth of the matter is that the accrued interest was already his; he could have discounted the coupon or, had he sold the bond, his receipts would have included the accrued interest.

variations. See *Griffiths* v. *Helvering,* No. 49, this Term, decided December 18, 1939; *Higgins* v. *Smith,* No. 146, this Term, decided January 8, 1940.

2. The question is one of considerable importance. The substantial conflict in decisions will inevitably result in confusion in the lower courts. And should the result below become accepted, taxpayers have obtained a ready means by which to escape the surtax rates without surrendering control of their propety.[5]

CONCLUSION

It is therefore respectfully submitted that this petition for a writ of certiorari should be granted.

FRANCIS BIDDLE,
Solicitor General.

MARCH 1940.

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[5] Tax services have already pointed out that the decision of the court below may be used to advantage by taxpayers. 1939 C. C. H., Vol. 1, pp. 461, 463; Alexander Tax News Letter, Vol. IV, No. 19, November 24, 1939. While it is true that there would be a gift tax on gifts of bond coupons amounting to more than $4,000, the gift tax would not reach gifts of less than that amount, and the donee in practically all cases would be in a lower surtax bracket than the donor.

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v.

PAUL R. G. HORST

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 14–19) is reported in 39 B. T. A. 757. The opinion of the Circuit Court of Appeals (R. 26–28) is reported in 107 F. (2d) 906.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered December 2, 1939 (R. 28). The petition for a writ of certiorari was filed March 2, 1940, and granted April 8, 1940 (R. 29). The jurisdiction of this Court rests on Section 240 (a)

of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The taxpayer owned coupon bonds. Several months prior to maturity of the interest coupons he detached them and gave them to his son, retaining the bonds themselves. Is he relieved of income tax with respect to such interest coupons?

STATUTE INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived * * * from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * * [U. S. C., Title 26, Sec. 22.]

STATEMENT

The facts, as stipulated (R. 22–24) and as found by the Board of Tax Appeals (R. 15), may be stated as follows:

The taxpayer, during the years 1934 and 1935, kept his books and made his income-tax returns on the cash receipts and disbursements basis (R. 15).

Throughout the year 1934 taxpayer owned certain coupon bonds. On August 10, 1934, he detached, prior to their maturity, negotiable interest coupons in the face amount of $25,182.50, and trans-

ferred them by manual delivery to his son, Robert P. K. Horst, as a gift. All of the coupons matured during the year 1934, and in that year the son collected the total amount due and reported it in his income-tax return for that year. (R. 15.)

Similarly, in August, 1935, he again detached interest coupons and gave them to his son, who collected $25,495 during that year on account of the coupons, and who reported that amount in his return [redacted][1] for 1935. (R. 15.)

The taxpayer did not report in his income tax returns for the years 1934 and 1935 any part of the amounts represented by the foregoing interest coupons. The Commissioner of Internal Revenue determined deficiencies for the years in question by adding $25,182.50 to gross income for 1934 and $22,360[1] for 1935 (R. 15).

The Board of Tax Appeals upheld the Commissioner's determination, with three members dissenting. The Circuit Court of Appeals reversed.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the owner of bonds need not include in his gross income an amount on account of the interest coupons which he detached and gave to his son several months prior to maturity.

2. In failing to hold that the owner of bonds should include the proceeds of the interest coupons

[1] He should have added $25,495 for 1935. The lower amount was undoubtedly an error.

in his gross income although he detached and gave them to his son several months prior to maturity.

3. In reversing the decision of the Board of Tax Appeals.

SUMMARY OF ARGUMENT

1. The owner of the bonds remained liable for income tax with respect to the interest thereon under the principles of *Helvering* v. *Clifford,* 309 U. S. 331. There, a taxpayer who had declared himself trustee of securities for five years to pay the income to his wife, reserving broad powers of management over the corpus, was held liable for tax with respect to the income which he had thus irrevocably set apart for his wife. The Court regarded as the "basic issue" whether or not "the grantor after the trust has been established may still be treated, under this statutory scheme, as the owner of the corpus." And the Court concluded that in view of the short duration of the trust, the retention of control over the corpus and the relationship between grantor and beneficiary, the husband should be treated as the owner of the corpus liable for tax upon the income therefrom.

The present case follows *a fortiori.* Here there was not even the interposition of a trust. The taxpayer continued to own the corpus outright, retaining all the powers of control which accompany ownership. Moreover, the short period of time between the gift of the interest coupons and their maturity more than matches the five year period in the *Clifford case.* And finally, the existence of a

close family relationship between grantor and beneficiary in the *Clifford* case is likewise present here.

The fact that the interest herein was embodied in separately disposable coupons should not make any difference. The beneficiary in the *Clifford* case similarly had an indefeasible right to income which she could readily assign. The transferability of the coupons by manual delivery may perhaps render assignability more dramatic in the present case, but the essential fact is that in both cases there was a complete alienation of the income by the taxpayer; and the considerations which required the taxpayer to remain accountable with respect to such income are all present here.

2. Moreover, the taxpayer is liable under the general rule that an assignor of income may not relieve himself of tax where he continues to own the underlying property that produces the income. This Court has held that the assignor of income from personal services remains liable for tax thereon. *Lucas* v. *Earl,* 281 U. S. 111. And in *Burnet* v. *Leininger,* 285 U. S. 136, the rule was extended to partnership income that was the product of *both* personal services and capital investment. Those two decisions have been cited by this Court as authority for the statement that "an assignment, where the assignor continued to own the corpus, does not immunize him from taxation upon the income" (*Reinecke* v. *Smith,* 289 U. S. 172, 177).

ARGUMENT

THE OWNER OF THE BONDS CONTINUED TO BE TAXABLE UNDER SECTION 22 (A) WITH RESPECT TO THE INTEREST COUPONS WHICH HE GAVE TO HIS SON

1. That the owner of the bonds could not relieve himself of tax with respect to the interest thereon simply by giving the coupons away shortly before their due date is clear, we submit, in the light of *Helvering* v. *Clifford,* 309 U. S. 331. There a husband declared himself trustee of certain securities to pay the income therefrom to his wife for five years. The trust was irrevocable, but the grantor retained broad powers of management. At termination, the corpus was to revert to him, while all accrued income was to go to his wife. He paid a gift tax upon the creation of the trust, and his wife reported in her separate returns all of the trust income distributed to her. This Court nevertheless held that the husband was taxable with respect to such income under Section 22 (a), notwithstanding that it had been distributed to another who was legally entitled to it. The Court regarded as the "basic issue" whether or not "the grantor after the trust has been established may still be treated, under this statutory scheme, as the owner of the corpus" (p. 334). And in holding the grantor taxable, the Court thus summarized the considerations which brought about that result (p. 335):

> the short duration of the trust, the fact that the wife was the beneficiary, and the retention of control over the corpus by respondent all lead irresistibly to the conclusion

that respondent continued to be the owner for purposes of § 22 (a).

The result in the instant case should follow *a fortiori* from the *Clifford* decision. Here there was not even the interposition of a trust. The father continued to own and control the corpus outright, without the necessity of going through the ritual of reserving broad powers of management as was done in the *Clifford* case. Again, the "short duration" of the trust, commented upon in the *Clifford* decision, is more than matched in this case. As against the five-year period in the *Clifford* case, there was here but a spread of several months between the gift of the interest and its due date. And finally, the close family relationship between grantor and beneficiary in the *Clifford* case finds its counterpart here in the fact that the object of the taxpayer's generosity was his son.

We respectfully submit that the instant case presents a far stronger case for the imposition of the tax. The taxpayer retained not merely broad powers over the corpus that might be translated into the substantial equivalent of ownership. He retained full ownership itself of the corpus, thereby resolving at the very outset the "basic issue" as it was posed in the *Clifford* decision.

There is, it is true, a single factual difference which the court below stressed in holding the tax invalid:[2] namely, that the income was embodied in

[2] The decision below was rendered prior to this Court's decision in the *Clifford* case.

negotiable coupons that were susceptible of separate ownership and control in the hands of the donee. We respectfully submit, however, that this difference is a purely formal one. The beneficiary in the *Clifford* case similarly had an indefeasible right to the income, a right which she could presumably assign, just as readily as the donee of the interest coupons could dispose of the latter by manual delivery. True, it may be more convenient to reassign the interest by the simple process of delivering the coupons, and it may perhaps be easier to find an assignee in view of the negotiable feature of the coupons, but these considerations do not detract from the single dominant fact which ties the cases together: there was just as complete and final alienation of the income in question in the *Clifford* case as there was here. The fact that the income here was identified with the separately disposable coupons may have rendered that alienation more dramatic, but it cannot obscure the common ground between the two cases. In both cases the owner of property about to receive income therefrom in the near future attempted to shift the incidence of the tax by deflecting the income to a member of his family without at the same time relinquishing his control over the property itself. It is difficult to believe that a different result should obtain by reason of a purely formal difference, particularly since all the other considerations in this case point even more strongly towards taxability.

In substance, the taxpayer simply made a gift of income to his son. Had he collected the interest

payments themselves and then paid over the proceeds to his son, or indeed, had he directed his son to collect the proceeds as his agent and to keep them as a gift, he would have remained liable.[3] Such technical variations upon the transaction which do not alter its practical substance should not produce diversity of tax consequences. Cf. *Griffiths* v. *Commissioner*, 308 U. S. 355; *Higgins* v. *Smith*, 308 U. S. 473.

2. In any event, since the gift of the coupons was simply an assignment of income, the donor is taxable under the general rule that an assignor of income cannot relieve himself of tax where he continues to own the underlying property that produces the income. The rule was plainly and unambiguously set forth by the Court in *Reinecke* v. *Smith*, 289 U. S. 172, where it stated (p. 177):

> This court has repeatedly said that such an assignment, where the assignor continued to own the corpus, does not immunize him from taxation upon the income. * * *

The Court then adverted to *Burnet* v. *Leininger*, 285 U. S. 136, and *Lucas* v. *Earl*, 281 U. S. 111.

Lucas v. *Earl* dealt with an assignment of income from personal services rather than income from

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[3] Indeed, under ordinary standards, the respondent made a gift to his son which was largely past rather than future income. The coupons were given one to four months in advance of maturity (R. 10). Although respondent kept his books upon a cash basis, the commercial truth of the matter is that the accrued interest was already his; he could have discounted the coupon, or had he sold the bond, his receipts would have reflected the accrued interest.

property. The assignment had been made nearly *twenty* years before the tax years in question. In holding the assignor taxable the Court declared (p. 114) that the case is "not to be decided by attenuated subtleties", and it refused to sanction an anticipatory arrangement (p. 115) "by which the fruits are attributed to a different tree from that on which they grew".

That the rule of *Lucas* v. *Earl* was not limited to assignments of income from personal services alone soon became apparent in *Burnet* v. *Leininger, supra.* In the *Leininger* case, the taxpayer, a partner in a laundry business, assigned [4] one-half of his interest to his wife, and thus attempted to avoid tax on one-half of his distributive income from the business. This Court held, however, that he nevertheless continued to remain taxable on the full amount of his distributive share.[5] But the income in the *Leininger* case arose from more than mere personal services. It was partnership income, a portion of which was undoubtedly *attributable to capital investment.* Although the personal efforts of the partner may have contributed towards the

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[4] Literally, the taxpayer attempted to make his wife an "equal partner" with him in his interest in the company. The Court, however, treated the situation simply as "an equitable assignment of one-half of what her husband should receive from the partnership". 285 U. S. at 141.

[5] See also *Balkwill* v. *Commissioner*, 77 F. (2d) 569 (C. C. A. 6th), certiorari denied, 296 U. S. 609; *Kasch* v. *Commissioner*, 63 F. (2d) 466 (C. C. A. 5th); *Rossmoore* v. *Commissioner*, 76 F. (2d) 520 (C. C. A. 2d).

production of that income, it flowed, in part at least, from property. The Court, however, drew no distinction between the two possible sources of income, but rather held broadly that the assignor remained liable. The Court in *Reinecke* v. *Smith, supra,* was therefore entirely justified in invoking the *Leininger* decision to support its statement that "an assignment, where the assignor continued to own the corpus, does not immunize him from taxation upon the income." Moreover, it is clear from a recent decision of this Court that neither the decision nor the language of the opinion in *Lucas* v. *Earl* is to be restricted to income from personal services. See *Griffiths* v. *Commissioner,* 308 U. S. 355, 358.

In holding that the taxpayer had succeeded in freeing himself of liability the court below relied upon *Blair* v. *Commissioner,* 300 U. S. 5. But that decision simply brings into striking relief the rule for which we are contending. There the assignor did not continue to own the property that gave rise to the income received by the assignee. The assignor originally owned an equitable life estate in property held in trust entitling him to all the net income derived from the property and then irrevocably parted with his entire interest in the property that produced the income received by the assignee. Here, on the other hand, the assignor continued to own the property which gave rise to the income in question—a distinction which is pivotal

if the foregoing decisions of this Court and their reasoning be accepted.[6]

3. The application of the principles established either by the *Clifford* case or by the assignment of income cases is particularly called for in view of the broad and comprehensive language of the statute. Section 22 (a) in all-inclusive terms defines gross income as including—

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[6] With minor exceptions the lower courts have repeatedly held that a taxpayer who assigns income from property while at the same time retaining the underlying property which produces that income does not relieve himself of tax with respect to that income. E. g., *Bing* v. *Bowers*, 22 F. (2d) 450, 454 (S. D. N. Y.), affirmed, 26 F. (2d) 1017 (C. C. A. 2d); *Porter* v. *United States*, 52 F. (2d) 1056 (C. Cls.); *Ward* v. *Commissioner*, 58 F. (2d) 757 (C. C. A. 9th), certiorari denied, 287 U. S. 656; *Wood* v. *Commissioner*, 74 F. (2d) 78 (C. C. A. 6th); *Helvering* v. *Gordon*, 87 F. (2d) 663 (C. C. A. 8th). See *Saenger* v. *Commissioner*, 69 F. (2d) 631, 632 (C. C. A. 5th). Cf. *Dickey* v. *Burnet*, 56 F. (2d) 917, 921 (C. C. A. 8th), certiorari denied, 287 U. S. 606.

In *Rosenwald* v. *Commissioner*, 33 F. (2d) 423 (C. C. A. 7th), certiorari denied, 280 U. S. 599, the taxpayer assigned about $830,000 income from rents, stocks and bonds. The court held about $815,000 thereof taxable to him, but relieved him of tax as to the remainder which represented bond coupons similar to those involved herein. Since the Government had prevailed as to the great bulk of the contested income, it did not apply for certiorari with respect to the relatively small amount attributable to the coupons. However, we believe that the distinction which the court drew between the assignment of income generally from property and the assignment of income represented by interest coupons is unsound. See discussion *supra*, p. 8. Cf. *Matchette* v. *Helvering*, 81 F. (2d) 73 (C. C. A. 2d), certiorari denied, 298 U. S. 677.

gains, profits, and income * * * growing out of the ownership or use of or interest in such property [or derived] from interest, rent, dividends, securities * * * or gains or profits and income derived from any source whatever.

l this Court has often said that the sweeping guage of those provisions indicates that it was purpose of Congress to use its power to the full ent. *Douglas* v. *Willcuts*, 296 U. S. 1, 9; *Irwin Gavit*, 268 U. S. 161; *Helvering* v. *Stockholms Bank*, 293 U. S. 84, 89; *United States* v. *Safety Heating Co.*, 297 U. S. 88, 93; *Helvering* v. *dland Ins. Co.*, 300 U. S. 216, 223; *Helvering* v. *fford*, 309 U. S. 331, 334. Cf. *Helvering* v. *uun*, 309 U. S. 461, 468.

CONCLUSION

The judgment of the court below should be ersed and that of the Board of Tax Appeals rmed.

Respectfully submitted.

FRANCIS BIDDLE,
Solicitor General.

SAMUEL O. CLARK, JR.,
Assistant Attorney General.

SEWALL KEY,
ARNOLD RAUM,
MORTON K. ROTHSCHILD,
Special Assistants to the Attorney General.

OCTOBER, 1940.

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FILE COPY

IN THE

Supreme Court of the United States

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No. [redacted] October Term, 1939

[illegible] T. Helvering, Commissioner of Internal Revenue,
Petitioner,

v.

Paul R. B. Hoser.

On Petition For a Writ of Certiorari to the United States Circuit Court of Appeals For the Second Circuit.

BRIEF FOR THE RESPONDENT IN OPPOSITION.

Harry H. Wiseman,
Attorney for Respondent.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1939

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

against

PAUL R. G. HORST.

On Petition For a Writ of Certiorari to the United States Circuit Court of Appeals For the Second Circuit.

BRIEF FOR THE RESPONDENT IN OPPOSITION.

Opinions Below.

Two opinions were delivered in the Board of Tax Appeals. Three members of the Board joined in a written dissent from the majority opinion. The majority opinion (R. 24) and the minority opinion (R. 31) are reported in 39 B. T. A. 757.

The opinion of the Circuit Court of Appeals (R. 46) is reported in 107 F. (2d) 906.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on December 2, 1939 (R. 49). The petition for certiorari was filed March 2, 1940. The jurisdiction of this Court is invoked by the Commissioner under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Question Presented.

The sole question presented is whether the taxpayer who detached coupons from bonds owned by him and delivered the coupons to another as a gift prior to their maturity is liable for income tax on the amounts thereafter collected on the coupons by the donee.

Statute Involved.

Revenue Act of 1934, c. 277, 48 Stat. 680:

> "SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—'Gross Income' includes gains, profits, and income derived * * * from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *" (U. S. S., Title 26, Sec. 22.)

Statement of Case.

The facts were stipulated and the Board of Tax Appeals adopted the stipulation (R. 39-43) as its findings of fact, which are substantially as follows (R. 25-26):

The taxpayer is a citizen of the United States. He kept his books and made his income tax returns on the cash basis (R. 25).

Throughout 1934 and 1935 the taxpayer was the owner of a number of coupon bonds (R. 25).

On August 10, 1934, the taxpayer detached unmatured coupons in the total amount of $25,182.50 and delivered them to his son as a gift. In August, 1935, the taxpayer made a similar gift to his son, involving unmatured coupons in the total amount of $37,032.50 (R. 25).

When the coupons matured, the son cashed them and included the proceeds in his income tax returns (R. 25-26).

The Commissioner, claiming that the proceeds were income to the taxpayer, added them to the taxable income of the taxpayer and determined a deficiency against the taxpayer for each year (R. 26).

The Board of Tax Appeals, three members dissenting, approved the Commissioner's determinations (R. 24-31).

The taxpayer appealed to the Circuit Court of Appeals for the Second Circuit, which reversed the Board's decision, holding that the amounts collected on the coupons were not income of the taxpayer (R. 46-48).

Argument.

I.

The Court below has held that the taxpayer is not liable for income tax on the amounts collected by his son on the coupons which the taxpayer, prior to their maturity, detached and delivered to his son as a gift. This decision

is in accord with applicable decisions of this Court and of the Circuit Courts of Appeals.

Negotiable interest coupons, when severed from the bonds to which they were originally attached and transferred to a person other than the owner and holder of the bonds, cease to be incidents of the bonds and become in fact separate and independent instruments, distinct from the bonds, and pass by delivery. They may be sold or made the subject of a gift *inter vivos.*

Clark v. *Iowa City,* 20 Wall 583;
Koshkonong v. *Burton,* 104 U. S. 668;
Clokey v. *Evansville & T. H. R. R. Co.,* 16 App. Div. 304;
Spooner v. *Holmes,* 102 Mass. 503;
Pratt v. *Higginson,* 230 Mass. 256;
Daniel on Negotiable Instruments, (7th ed. (1933) Vol. 3, p. 1919, Sec. 1873).

This Court, in *Clark* v. *Iowa City* (20 Wall. 583), *supra,* stated the rule as follows (p. 589):

> "These coupons, when severed from the bonds, are negotiable and pass by delivery. They then cease to be incidents of the bonds, and become in fact independent claims; they do not lose their validity, if for any cause the bonds are cancelled or paid before maturity; nor their negotiable character; nor their ability to support separate actions, and the amount for which they are issued draws interest from its maturity. They then, possess the essential attributes of commercial paper, as has been held by this court in repeated instances.
>
> • • • • • • • • • •
>
> "Coupons, when severed from the bonds to which they were originally attached, are in legal effect equiv-

alent to separate bonds for the different installments of interest. The like action may be brought upon each of them, when they respectively become due, as upon the bond itself when the principal matures; * * *."

When the taxpayer detached the unmatured coupons and delivered them to his son as a gift, "the donee acquired title to a severable part of each of the original instruments; the part which carried the right to receive the payment in question, free from the interference or assistance of the donor, and without regard to what disposition was made of the remainder of the instrument".

Williston v. *Commissioner,* 2 Mass. A. T. B. 663; Cases, supra.

The amounts collected on the coupons by the donee were the donee's income, not the income of the donor, as it was subject to the unfettered command of the donee, not subject to any power of control over it exercisable by the donor; the source of it being severable parts of the original instruments carrying the right to receive the interest thereon for stated periods and irrevocably vested in the donee.

Cf. United States v. *First National Bank of Birmingham* (C. C. A. 5) 74 F. (2d) 360.

The income in question was not taxable to the taxpayer because he did not control it, or receive it, or own it, or have any beneficial interest therein. "The one who is to receive the income as the owner of the beneficial interest is to pay the tax".

Blair v. *Commissioner,* 300 U. S. 5.

The Court below followed the decision of the Circuit Court of Appeals for the Seventh Circuit in *Rosenwald* v. *Commissioner,* 33 F. (2d) 423,[1] where the precise question here presented was decided against the Commissioner. There the taxpayer clipped negotiable interest coupons from Third Liberty Loan bonds and delivered the coupons to a donee prior to maturity. The donee collected the interest due on the coupons at maturity. It was held that the interest collected on the coupons by the donee was not taxable as income to the taxpayer.

This Court decided that the question here presented is one which it will not review when it denied the Commissioner's petition for a writ of certiorari in *Matchette* v. *Helvering,* (C. C. A. 2), 81 F. (2d) 73, certiorari denied, 298 U. S. 677, where it was held that a stockholder who made an outright assignment of a dividend after the date of declaration but before the date of payment was not taxable on the dividend.

The Massachusetts Appellate Tax Board, in *Williston* v. *Commissioner* (2 Mass. A. T. B. 663), *supra*[2], where the facts were identical with those in this case, citing the Board's decision in this case, but refusing to be persuaded by it, reached the same conclusion as the Court below a few months before the decision below was handed down.

The alleged conflict of decision (Pet. 5) does not exist. In *Helvering* v. *Clifford,* No. 383, this term, decided Febru-

[1] The taxpayer's petition for a writ of certiorari in this case was denied (280 U. S. 599). The Commissioner, then, did not think enough of the point that he is now urging to seek a review in this Court of the decision against him.

[2] This case is now pending on appeal in the Supreme Judicial Court of Massachusetts.

ary 26, 1940, this Court held that on the facts of the case the taxpayer, who was the grantor of an irrevocable, short term trust, remained, for the purposes of section 22(a) of the Revenue Act of 1934, the owner of the trust corpus. "In view of this result," the Court said, "we need not examine the contention that the trust device falls within the rule of *Lucas* v. *Earl*, 281 U. S. 111 and *Burnet* v. *Leininger*, 285 U. S. 136, relating to the assignment of future income; • • •". The *Clifford* decision, therefore, does not touch the question here presented.

Nor has the Court below ignored the doctrine of *Lucas* v. *Earl* (281 U. S. 11), *supra*, and *Burnet* v. *Leininger* (285 U. S. 136), *supra*. The Commissioner invoked the doctrine of those cases in this Court in *Blair* v. *Commissioner* (300 U. S. 5), *supra*, only to learn that that doctrine was limited in its application to the assignment of future personal earnings and did not apply to the assignment by a father to his children of beneficial interests in the income of a testamentary trust. As this Court there pointed out (pp. 11-12):

> "These cases (Lucas v. Earl and Burnet v. Leininger) are not in point. The tax here is not upon earnings which are taxed to the one who earns them."
> • • • • • • • • • •
> "In the instant case, the tax is upon income as to which, in the general application of the revenue acts, the tax liability attaches to ownership."

The Commissioner cites a list of cases in which, he says, "the Circuit Courts of Appeals have consistently held that unless the taxpayer assigns the corpus which produces the income, he cannot by assignment of future income be relieved of taxation on that income" (Pet. 6-7). Among the cases cited is *Rosenwald* v. *Commissioner* (33 F. [2d] 423,

certiorari denied, 280 U. S. 599), *supra*, which does in fact support the Commissioner's contention. It is that very case, however, which draws the distinction that takes this case out of the rule which the Commissioner seeks to apply here.

The Commissioner says that the taxpayer "clearly would be taxable on the amount of the bond coupons if he had collected the interest payments before giving the proceeds to his son; or, indeed, if he had directed the son to collect the coupons as his agent and to keep the proceeds as a gift" (Pet. 7).

This would undoubtedly be true, but the taxpayer did not do either of these things any more than did the taxpayer in *Blair* v. *Commissioner* (300 U. S. 5), *supra*, when he assigned to his children beneficial interests in the income of a testamentary trust.

Conclusion.

The decision below is correct. There is no conflict of decision, but, on the contrary, there is unanimity of decision; and besides, this Court has already decided that the question here presented is one which it will not review. It follows, therefore, that the petition for a writ of certiorari should be denied.

Respectfully submitted,

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March, 1940.

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No. 27

IN THE

Supreme Court of the United States

October Term, 1940.

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

against

PAUL R. G. HORST,
Respondent.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

BRIEF FOR THE RESPONDENT.

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BRIEF FOR RESPONDENT.

Opinions Below.

The opinions below are those of the Board of Tax Appeals, reported in 39 B. T. A. 757, printed in the record herein at pages 14-19; and that of the Circuit Court of Appeals, reported in 107 F. (2d) at page 906, printed in the record herein at pages 26-28.

Jurisdiction of this Court.

The jurisdiction of this Court arises under Section 240 (a) of the Judicial Code and this Court's grant of a writ of certiorari herein on April 8, 1940.

Statement of the Case.

This case presents a single question, arising out of two income tax returns of the respondent, one for the year 1934, the other for the year 1935.

On August 10, 1934, the respondent detached from various coupon bonds he owned negotiable interest coupons amounting to $25,182.50, maturing respectively from five to sixteen weeks later, and then made an outright gift of these coupons to his son, who later in 1934 collected these coupons as they matured and reported them in his own return for 1934 as part of his own income for that year (R. 15).

In 1935 the respondent made a similar gift to his son of similar unmatured coupons cut by respondent from bonds he owned. These 1935 coupons had a par value of $37,032.50, but only $25,495.00 was collected thereon by the son, who reported the amount collected therefrom in his own income tax return for that year (R. 15).

The respondent, whose returns were made each year on a cash basis (R. 15), did not report in either year as part of his own income the amount of these coupons which he had so given away before their maturity (R. 15).

The Commissioner later assessed deficiencies in income against the respondent on account of these coupons of $25,182.50 for 1934 and of $22,360.00* for 1935, on the

* The difference between the $25,495 reported by the son and the $22,360 deficiency assessed against the respondent is apparently due to some offsetting items credited to the respondent by the Commissioner (R. 15).

sole ground that the bonds themselves had not been transferred to the son with the coupons (R. 6 and 11). Corresponding deficiencies in tax were assessed by the Commissioner against the respondent of $13,903.09 and interest for 1934 (R. 12) and of $12,376.20 and interest for 1935 (R. 6).

The respondent petitioned the Board of Tax Appeals for review of these several deficiency assessments. The Board statedly declined to follow the decision of the Circuit Court of Appeals for the Seventh Circuit in *Rosenwald* v. *Commissioner,* 33 F. (2d) 423, an identical case (R. 16); and sustained the ruling of the Commissioner (R. 18).

Three members of the Board, however, dissented from its ruling (R. 18-19).

The respondent then appealed to the Circuit Court of Appeals for the Second Circuit, which unanimously reversed the order of the Board of Tax Appeals.

The Circuit Court of Appeals cited in support of its decision the *Rosenwald* case (33 F. (2d) 423), and its own earlier decision in *Matchette* v. *Helvering,* 81 F. (2d) 73, and distinguished the cases on which the petitioner relied, on the basis that the gift of the coupons in this case was an outright completed gift of a separate piece of property, not dependent on any further act of the donor, or even on the donor's continuing to hold the bonds.

The Court below pointed out, too, that in such cases as *Lucas* v. *Earl,* 281 U. S. 111; *Burnett* v. *Leininger,* 285 U. S. 136 and *Bing* v. *Bowers,* 22 F. (2d) 450 and 26 F. (2d) 1017, the future income given away was not independent

and completely severed from the principal, as is the case with the coupons in the case at bar, but was dependent in each instance on future acts of the donor; in the *Lucas* case on his subsequent earnings, in *Burnet* v. *Leininger* on his continuing in a partnership, in *Bing* v. *Bowers* because the donor had given up no interest in the land, had created no rent charge thereon, and had in fact retained control over the net income he had purported to grant to another (R. 28).

It mentioned, too, that this Court had itself pointed out this distinction in *Blair* v. *Commissioner*, 300 U. S. 5 (R. 28).

Subsequently this Court decided the case of *Helvering* v. *Clifford*, 309 U. S. 331, on which the petitioner principally relies, and which seems to us inapplicable to the case at bar.

Summary of the Argument.

The controlling facts in the case at bar are that the unmatured coupons given outright by the respondent to his son were independent negotiable instruments; that they never became income of the respondent, who made his returns on the cash basis; and that the respondent's retention of the bonds, shorn of the coupons, left to the respondent no vestige of ownership or control over the coupons so given away by him.

The decisions of the two different Circuit Courts of Appeal which have passed on the point presented agree that the coupons so given away before maturity are not income of the donor.

The case differs materially in its essentials from that presented in *Helvering* v. *Clifford,* 309 U. S. 331, and the decision in the case at bar is supported by this court's decision in *Blair* v. *Commissioner,* 300 U. S. 5, 11-14.

ARGUMENT.

I.

The coupons given by the respondent to his son before their maturity were independent negotiable instruments complete in themselves, and by the gift became the absolute property of the donee free from any control by the donor by reason of his retention of the bonds from which they had been detached.

Clark v. *Iowa City,* 20 Wall. 583;
Hartman v. *Greenhow,* 102 U. S. 672;
Koshkonong v. *Burton,* 104 U. S. 668;
Clokey v. *Evansville & T. H. R. R. Co.* 16 App. Div. 304;
Pratt v. *Higginson,* 230 Mass. 256.

This long settled doctrine—the controlling feature of the present case—is dealt with by the petitioner in the most casual manner by the statement in his brief

> "The fact that the interest herein was embodied in separately disposable coupons should not make any difference." (Petitioner's Brief, p. 5)

and the subsequent statement:

> "We respectfully submit that the difference is a purely formal one." (Petitioner's Brief, p. 8)

In our view, this difference between absolute and merely contingent ownership is both substantial and controlling. And so it has appeared, on another occasion, to the Commissioner, who ruled in 1939 that a purchaser of unmatured coupons must pay income tax on whatever he collected above what he paid for the coupons.

I. T. 3312, C. B. 1939-2, 168.

And in this particular instance the donee reported the entire amount collected as his income (R. 15).

II.

The two cases on this point in the Circuit Courts of Appeal agree that coupons so given away before their maturity are not income of the donor, but of the donee.

Rosenwald v. *Commissioner,* 33 F. (2d) 423;
Horst v. *Commissioner,* 107 F. (2d) 906;

See also, for similar rulings:

Matchette v. *Helvering,* 81 F. (2d) 73;
Williston v. *Commissioner,* 2 Mass. A. T. B. 663;
Schoonmaker v. *Commissioner,* 39 B. T. A. 496;
I. T. 3312, C. B. 1939-2, 168.

III.

The case at bar does not come within the doctrines laid down in *Helvering* v. *Clifford*, 309 U. S. 331, but within those declared in *Blair* v. *Commissioner*, 300 U. S. 5, 11-14.

Subsequent to the decision of the present case by the Circuit Court of Appeals, this Court handed down its decision in the case of *Helvering* v. *Clifford*, 309 U. S. 331, on which the petitioner places his main reliance.

Several features of the *Clifford* case distinguish it sharply from the case at bar, though apparently these crucial differences have not impressed counsel for the petitioner.

In the *Clifford* case there were the following striking features, none of which exist in the case at bar:

There was there no separate thing separated and completely transferred.

What was transferred there, and that only *sub modo*, was net income from a trust fund over which Mr. Clifford retained absolute control. He might easily, under the extensive powers reserved to himself, invest it in such a way that there might be no net income therefrom during the specified period. That was left to his own absolute discretion. That is a very different thing from an absolute transfer of a specific coupon.

Moreover, in the *Clifford* case, Mr. Clifford also retained control even over whatever net income there might be, under the striking provision that he was to pay over to his wife during the continuance of the trust, the whole

or such part of the net income as he "in his absolute discretion" might determine. That provision practically nullified any absolute right on her part to get the income.

Raymond v. *Tiffany*, 59 Misc. 283.

Any income paid her became a completed gift only when Mr. Clifford exercised his discretion in her favor, after the income had been collected by him.

This Court, in its opinion in the *Clifford* case, further pointed out that Mr. Clifford "retained the substance of "full enjoyment of all the rights which previously he had "in the property." (309 U. S. 331, 336.)

As this Court indicated in its opinion in the *Clifford* case, it was the combination of all the elements appearing in that case that constituted the appropriate foundation for the finding there sustained (309 U. S. 331, 336).

The situation here is radically different. The coupons given by Mr. Horst were separate negotiable instruments.

Clark v. *Iowa City*, 20 Wall. 583;
Hartman v. *Greenhow*, 102 U. S. 672;
Koshkonong v. *Burton*, 104 U. S. 668.

Mr. Horst had parted with them absolutely and completely, before their maturity.

His ownership of the bonds, shorn of their coupons, gave him not the slightest control over the donated coupons.

He could sell or give the bonds, without the donated coupons, to some third person, and such third person would have no more control over the donated coupons than he himself had.

He could, if he wished, destroy the bonds from which the coupons had been clipped, but the coupons would none the less remain valid in the hands of his donee totally unaffected by what he did with or to the bonds from which they had been detached.

In a parallel case before the Massachusetts Appellate Tax Board under the similar Massachusetts Statute it was pointed out, orally (as we are informed by counsel in that case), that if the donor gave the unmatured coupons to one, and gave the bond without the coupons to another, there would certainly be difficulty about charging the separate donee of the bond with the income collected on the coupon, and no answer to the suggestion was forthcoming.

The Massachusetts Board, in a studied opinion, declined to tax the owner of the naked bonds with the income received by his donee of the coupons.

Williston v. *Commissioner,* 2 Mass. A. T. B. 663.

In a footnote to page 9 of his brief, the petitioner suggests, as he suggested orally in the Circuit Court of Appeals, that the donor, if he made his returns on the accrual basis, might perhaps have been taxed on the accrual on the coupons up to the time of gift. The answer, of course, is that he made his returns on the cash basis, and did not receive any of that accruing income.

It was suggested on the argument of this case before the Circuit Court of Appeals that this respondent might have sold the coupons at a discount, and this petitioner was asked by the Court: "On what amount would you then tax him?" The answer was, and had to be, on the amount he got for them. So to the following question: "And when

he got nothing for them, on what would you tax him?'' the petitioner had no answer to offer.

The Commissioner had already ruled that the transferee of the coupon must report as his own income the amount collected thereon, less what he had paid for the coupon.

I. T. 3312, C. B. 1939-2, 168.

The entire argument for the petitioner seeks to ignore the fundamental fact that the coupon is a wholly independent and separate obligation from the bond, which, when parted with, is entirely beyond the control of the owner of the bond.

The retention of some remaining control over the coupon by the owner of the bond would be of the essence of the case to bring it within the principles of any of the decisions on which the petitioner relies. Here the gift was absolute, leaving no vestige of any such control.

There is but little to add to the argument set forth in the opinion of the Circuit Court of Appeals.

Counsel for the petitioner have twice quoted a phrase from this Court's opinion in *Reinecke* v. *Smith,* 289 U. S. 172, 177. The first time they quoted it (on page 5 of their brief) they omitted the controlling word ''such'' with which the phrase opened. The second time (on page 9 of their brief) they kept the word ''such'' in, but omitted to mention what that restrictive word referred to. They have thus apparently given to that quotation a force which does not belong to it, and which this Court later rejected as a misconstruction of it.

Blair v. *Commissioner,* 300 U. S. 5, 11-14.

The case at bar comes directly within that last cited decision.

IV.

The decision of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

HARRY H. WIGGINS,
Attorney for Respondent.

SELDEN BACON,
Of Counsel.

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SUPREME COURT OF THE UNITED STATES.

No. 27.—October Term, 1940.

Guy T. Helvering, Petitioner,
vs.
Paul R. G. Horst.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[November 25, 1940.]

Mr. Justice Stone delivered the opinion of the Court.

The sole question for decision is whether the gift, during the donor's taxable year, of interest coupons detached from the bonds, delivered to the donee and later in the year paid at maturity, is the realization of income taxable to the donor.

In 1934 and 1935 respondent, the owner of negotiable bonds, detached from them negotiable interest coupons shortly before their due date and delivered them as a gift to his son who in the same year collected them at maturity. The Commissioner ruled that under the applicable § 22 of the Revenue Act of 1934, 48 Stat. 680, 686, the interest payments were taxable, in the years when paid, to the respondent donor who reported his income on the cash receipts basis. The circuit court of appeals reversed the order of the Board of Tax Appeals sustaining the tax. 107 F. (2d) 906; 39 B. T. A. 757. We granted certiorari, 309 U. S. 650, because of the importance of the question in the administration of the revenue laws and because of an asserted conflict in principle of the decision below with that of *Lucas* v. *Earl*, 281 U. S. 111, and with that of decisions by other circuit courts of appeals. See *Bishop* v. *Commissioner*, 54 F. (2d) 298; *Dickey* v. *Burnet*, 56 F. (2d) 917, 921; *Van Meter* v. *Commissioner*, 61 F. (2d) 817.

The court below thought that as the consideration for the coupons had passed to the obligor, the donor had, by the gift, parted with all control over them and their payment, and for that reason the case was distinguishable from *Lucas* v. *Earl*, *supra* and *Burnet* v. *Leininger*, 285 U. S. 136, where the assignment of compensation for services had preceded the rendition of the services, and where the income was held taxable to the donor.

The holder of a coupon bond is the owner of two independent and separable kinds of right. One is the right to demand and receive at maturity the principal amount of the bond representing capital investment. The other is the right to demand and receive interim payments of interest on the investment in the amounts and on the dates specified by the coupons. Together they are an obligation to pay principal and interest given in exchange for money or property which was presumably the consideration for the obligation of the bond. Here respondent, as owner of the bonds, had acquired the legal right to demand payment at maturity of the interest specified by the coupons and the power to command its payment to others which constituted an economic gain to him.

Admittedly not all economic gain of the taxpayer is taxable income. From the beginning the revenue laws have been interpreted as defining "realization" of income as the taxable event rather than the acquisition of the right to receive it. And "realization" is not deemed to occur until the income is paid. But the decisions and regulations have consistently recognized that receipt in cash or property is not the only characteristic of realization of income to a taxpayer on the cash receipts basis. Where the taxpayer does not receive payment of income in money or property realization may occur when the last step is taken by which he obtains the fruition of the economic gain which has already accrued to him. *Old Colony Trust Co.* v. *Commissioner,* 279 U. S. 716; *Corliss* v. *Bowers,* 281 U. S. 376, 378. Cf. *Burnet* v. *Wells,* 289 U. S. 670.

In the ordinary case the taxpayer who acquires the right to receive income is taxed when he receives it, regardless of the time when his right to receive payment accrued. But the rule that income is not taxable until realized has never been taken to mean that the taxpayer, even on the cash receipts basis, who has fully enjoyed the benefit of the economic gain represented by his right to receive income, can escape taxation because he has not himself received payment of it from his obligor. The rule, founded on administrative convenience, is only one of postponement of the tax to the final event of enjoyment of the income, usually the receipt of it by the taxpayer, and not one of exemption from taxation where the enjoyment is consummated by some event other than the taxpayer's personal receipt of money or property. Cf. *Aluminum Castings Co.* v. *Routzahn,*

282 U. S. 92, 98. This may occur when he has made such use or disposition of his power to receive or control the income as to procure in its place other satisfactions which are of economic worth. The question here is, whether because one who in fact receives payment for services or interest payments is taxable only on his receipt of the payments, he can escape all tax by giving away his right to income in advance of payment. If the taxpayer procures payment directly to his creditors of the items of interest or earnings due him, see *Old Colony Trust Co.* v. *Commissioner, supra; Bowers* v. *Kerbaugh Empire Co.*, 271 U. S. 170; *United States* v. *Kirby Lumber Co.*, 284 U. S. 1, or if he sets up a revocable trust with income payable to the objects of his bounty, §§ 166, 167, Revenue Act of 1934, *Corliss* v. *Bowers, supra;* cf. *Dickey* v. *Burnet*, 56 F. (2d) 917, 921, he does not escape taxation because he did not actually receive the money. Cf. *Douglas* v. *Willcuts*, 296 U. S. 1; *Helvering* v. *Clifford*, 309 U. S. 331.

Underlying the reasoning in these cases is the thought that income is "realized" by the assignor because he, who owns or controls the source of the income, also controls the disposition of that which he could have received himself and diverts the payment from himself to others as the means of procuring the satisfaction of his wants. The taxpayer has equally enjoyed the fruits of his labor or investment and obtained the satisfaction of his desires whether he collects and uses the income to procure those satisfactions, or whether he disposes of his right to collect it as the means of procuring them. Cf. *Burnet* v. *Wells, supra.*

Although the donor here, by the transfer of the coupons, has precluded any possibility of his collecting them himself he has nevertheless, by his act, procured payment of the interest, as a valuable gift to a member of his family. Such a use of his economic gain, the right to receive income, to procure a satisfaction which can be obtained only by the expenditure of money or property, would seem to be the enjoyment of the income whether the satisfaction is the purchase of goods at the corner grocery, the payment of his debt there, or such non-material satisfactions as may result from the payment of a campaign or community chest contribution, or a gift to his favorite son. Even though he never receives the money he derives money's worth from the disposition of the coupons which he has used as money or money's worth in the procuring of a satis-

faction which is procurable only by the expenditure of money or money's worth. The enjoyment of the economic benefit accruing to him by virtue of his acquisition of the coupons is realized as completely as it would have been if he had collected the interest in dollars and expended them for any of the purposes named. *Burnet* v. *Wells, supra.*

In a real sense he has enjoyed compensation for money loaned or services rendered and not any the less so because it is his only reward for them. To say that one who has made a gift thus derived from interest or earnings paid to his donee has never enjoyed or realized the fruits of his investment or labor because he has assigned them instead of collecting them himself and then paying them over to the donee, is to affront common understanding and to deny the facts of common experience. Common understanding and experience are the touchstones for the interpretation of the revenue laws.

The power to dispose of income is the equivalent of ownership of it. The exercise of that power to procure the payment of income to another is the enjoyment and hence the realization of the income by him who exercises it. We have had no difficulty in applying that proposition where the assignment preceded the rendition of the services, *Lucas* v. *Earl, supra; Burnet* v. *Leininger, supra,* for it was recognized in the *Leininger* case that in such a case the rendition of the service by the assignor was the means by which the income was controlled by the donor and of making his assignment effective. But it is the assignment by which the disposition of income is controlled when the service precedes the assignment and in both cases it is the exercise of the power of disposition of the interest or compensation with the resulting payment to the donee which is the enjoyment by the donor of income derived from them.

This was emphasized in *Blair* v. *Commissioner,* 300 U. S. 5, on which respondent relies, where the distinction was taken between a gift of income derived from an obligation to pay compensation and a gift of income-producing property. In the circumstances of that case the right to income from the trust property was thought to be so identified with the equitable ownership of the property from which alone the beneficiary derived his right to receive the income and his power to command disposition of it that a gift of the income by the beneficiary became effective only as a gift of his ownership of the property producing it. Since the gift was deemed

to be a gift of the property the income from it was held to be the income of the owner of the property, who was the donee, not the donor, a refinement which was unnecessary if respondent's contention here is right, but one clearly inapplicable to gifts of interest or wages. Unlike income thus derived from an obligation to pay interest or compensation, the income of the trust was regarded as no more the income of the donor than would be the rent from a lease or a crop raised on a farm after the leasehold or the farm had been given away. *Blair* v. *Commissioner, supra,* 12, 13 and cases cited. See also *Reinecke* v. *Smith,* 289 U. S. 172, 177. We have held without deviation that where the donor retains control of the trust property the income is taxable to him although paid to the donee. *Corliss* v. *Bowers, supra.* Cf. *Helvering* v. *Clifford, supra.*

The dominant purpose of the revenue laws is the taxation of income to those who earn or otherwise create the right to receive it and enjoy the benefit of it when paid. See, *Corliss* v. *Bowers, supra,* 378; *Burnet* v. *Guggenheim,* 288 U. S. 280, 283. The tax laid by the 1934 Revenue Act upon income "derived from . . . wages or compensation for personal service, of whatever kind and in whatever form paid, . . . ; also from interest . . . " therefore cannot fairly be interpreted as not applying to income derived from interest or compensation when he who is entitled to receive it makes use of his power to dispose of it in procuring satisfactions which he would otherwise procure only by the use of the money when received.

It is the statute which taxes the income to the donor although paid to his donee. *Lucas* v. *Earl, supra; Burnet* v. *Leininger, supra.* True, in those cases the service which created the right to income followed the asignment and it was arguable that in point of legal theory the right to the compensation vested instantaneously in the assignor when paid although he never received it; while here the right of the assignor to receive the income antedated the assignment which transferred the right and thus precluded such an instantaneous vesting. But the statute affords no basis for such "attenuated subtleties." The distinction was explicitly rejected as the basis of decision in *Lucas* v. *Earl.* It should be rejected here, for no more than in the *Earl* case can the purpose of the statute to tax the income to him who earns, or creates and enjoys it be es-

caped by "anticipatory arrangements however skilfully devised" to prevent the income from vesting even for a second in the donor.

Nor is it perceived that there is any adequate basis for distinguishing between the gift of interest coupons here and a gift of salary or commissions. The owner of a negotiable bond and of the investment which it represents, if not the lender, stands in the place of the lender. When, by the gift of the coupons, he has separated his right to interest payments from his investment and procured the payment of the interest to his donee, he has enjoyed the economic benefits of the income in the same manner and to the same extent as though the transfer were of earnings and in both cases the import of the statute is that the fruit is not to be attributed to a different tree from that on which it grew. See *Lucas* v. *Earl, supra,* 115.

Reversed.

A true copy.

Test:

Clerk, Supreme Court, U. S.

SUPREME COURT OF THE UNITED STATES.

No. 27.—October Term, 1940.

Guy T. Helvering, Petitioner,
vs.
Paul R. G. Horst.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[November 25, 1940.]

The separate opinion of Mr. Justice McReynolds.

The facts were stipulated. In the opinion of the court below the issues are thus adequately stated—

"The petitioner owned a number of coupon bonds. The coupons represented the interest on the bonds and were payable to bearer. In 1934 he detached unmatured coupons of face value of $25,182.50 and transferred them by manual delivery to his son as a gift. The coupons matured later on in the same year, and the son collected the face amount, $25,182.50, as his own property. There was a similar transaction in 1935. The petitioner kept his books on a cash basis. He did not include any part of the moneys collected on the coupons in his income tax returns for these two years. The son included them in his returns. The Commissioner added the moneys collected on the coupons to the petitioner's taxable income and determined a tax deficiency for each year. The Board of Tax Appeals, three members dissenting, sustained the Commissioner, holding that the amounts collected on the coupons were taxable as income to the petitioner."

The decision of the Board of Tax Appeals was reversed and properly so, I think.

The unmatured coupons given to the son were independent negotiable instruments, complete in themselves. Through the gift they became at once the absolute property of the donee, free from the donor's control and in no way dependent upon ownership of the bonds. No question of actual fraud or purpose to defraud the revenue is presented.

Neither *Lucas* v. *Earl*, 281 U. S. 111, nor *Burnet* v. *Leininger*, 285 U. S. 136, support petitioner's view. *Blair* v. *Commissioner*, 300

U. S. 5, 11, 12, shows that neither involved an unrestricted completed transfer of property.

Helvering v. *Clifford*, 309 U. S. 331, 335, 336, decided after the opinion below, is much relied upon by petitioner, but involved facts very different from those now before us. There no separate thing was absolutely transferred and put beyond possible control by the transferror. The court affirmed that Clifford, both conveyor and trustee, "retained the substance of full enjoyment of all the rights which previously he had in the property." "In substance his control over the corpus was in all essential respects the same after the trust was created as before." "With that control in his hands he would keep direct command over all that he needed to remain in substantially the same financial situation as before."

The general principles approved in *Blair* v. *Commissioner*, 300 U. S. 5, are applicable and controlling. The challenged judgment should be affirmed.

The CHIEF Justice and Mr. Justice ROBERTS concur in this opinion.

END